

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 ird.govt.nz/subscription-service/subscription-form to receive regular email updates when we publish new draft items for comment.

Ref	Draft type	Title	Comment deadline
PUB00515	Interpretation statement	GST treatment of supplies of payment processing or facilitation services to merchants	8 December 2025
PUB00513	Interpretation statement	Working for Families tax credits and family scheme income	9 December 2025
PUB00507	Question we've been asked	When does the fringe benefit tax exclusion for benefits relating to health or safety apply?	12 December 2025
PUB00501	Interpretation statement	Tax Administration – shortfall penalties	15 December 2025
PUB00470	Interpretation statement	Income tax – payments by employers on the death of an employee to executors and family	30 January 2026

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FINAL ISSUE FOR 2025

This is the final issue of the Tax Information Bulletin for 2025. The next issues will be in February 2026.

IN SUMMARY

Determination

FDR 2025/06: Determination the fair dividend rate method may not be used to calculate FIF income by investors in the Nuveen Global Sustainable Bond Fund – Class X NZD Distributing (H) share class

3

Subject to the conditions recorded below, any investment by a New Zealand resident investor in the Class X NZD Distributing Hedge share class of the Nuveen Global Sustainable Bond Fund, (ISIN IE000RJY9QW0) a sub-fund of Nuveen Global Investors Fund Public Limited Company ("Nuveen GIF"), to which none of the exemptions in sections EX 29 to 43 of the Income Tax Act 2007 apply, is a type of attributing interest for which the investor may not use the fair dividend rate ("FDR") method to calculate foreign investment fund income for the interest.

Binding Rulings

BR Prd 25/05: Ministry of Education

6

The Arrangement is the payment of bursaries that Initial Teacher Education (ITE) providers make to eligible student teachers under the School Onsite Training Programme. To be eligible, student teachers must be hosted in schools 3 days a week while completing their 1-year graduate or postgraduate ITE programme, approved by the Teaching Council, that will lead to teacher registration.

BR Prd 22/06: Ministry of Education

9

The Arrangement is the payment of bursaries that the Ministry of Education makes to eligible student teachers under the Go Rural: Isolated Placements Fund. The bursaries are awarded to student teachers who are hosted in an isolated or rural, state or state-integrated school while completing their Initial Teacher Education programme that is Teaching Council approved.

Interpretation statements

IS 25/22: GST – Secondhand goods input tax deduction

11

This interpretation statement discusses the requirements that must be met for a registered person to claim a secondhand goods input tax deduction. This includes, among other things, a discussion of the requirement that the goods be secondhand and the meaning of secondhand.

IS 25/23: GST – Meaning of payment

42

This interpretation statement discusses the meaning of "payment" for GST purposes. The meaning of payment is relevant for determining the time of supply, the tax period for which you return output tax or for which you claim an input tax deduction, and eligibility for a secondhand goods input tax deduction.

IS 25/24: Income tax and GST – industries other than forestry registered in the Emissions Trading Scheme

55

This interpretation statement applies to industries registered in the Emissions Trading Scheme, other than forestry which is taxed differently. The industries include those that are emissions intensive and trade exposed, as well as those involved in removal activities and some horticultural activities. The statement sets out the conceptual framework for the income tax treatment of emission liabilities and emissions units (NZUs) in these sectors. It then explains how to calculate deductions for emission liabilities and it discusses the treatment of NZUs as income. Finally, there is a brief discussion of the GST treatment of NZUs.

IS 25/25: Income tax – business activity

86

This interpretation statement gives guidance on whether and when a taxpayer is carrying on a "business" for income tax purposes. This is relevant to whether a person has income from a business under s CB 1 and to other provisions in the Income Tax Act 2007 where carrying on a business is a requirement.

IN SUMMARY

Question we've been asked

QB 25/21: Income tax – Public private partnership projects and business continuity test for losses

115

This QWBA confirms that s IB 3(2)(c), which is a central requirement of the business continuity test, is not breached when a standard PPP project transitions from the design and construction phase to the operation and maintenance phase. Accordingly, a corporate PPP contractor may generally rely on the business continuity test to carry forward losses incurred during the design and construction phase, even if shareholder continuity is breached during that phase.

Technical decision summaries

TDS 25/24: The supply of accommodation in a serviced apartment

121

This item summarises a private ruling about the supply of accommodation in a retirement village that includes the provision of mandatory services and whether this constitutes the taxable supply of accommodation in a commercial dwelling.

TDS 25/25: Restructure and transfer of shares

124

This item summarises a private ruling about the transfer of shares between companies within a group as part of a restructure and whether any future sale of the shares is taxable.

TDS 25/26: How does the business continuity test apply to a consolidated group?

126

This item summarises a private ruling about the exit of two company subsidiaries from a consolidated group and the sale of a third subsidiary (the sole remaining member of the consolidated group) to a third party. It considers the business continuity test and whether a specific anti-avoidance provision applies.

LEGISLATION AND DETERMINATION

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.

FDR 2025/05: Determination the fair dividend rate method may not be used to calculate FIF income by investors in the Nuveen Global Sustainable Bond Fund – Class X NZD Distributing (H) share class

Subject to the conditions recorded below, any investment by a New Zealand resident investor in the Class X NZD Distributing Hedge share class of the Nuveen Global Sustainable Bond Fund, (ISIN IE000RJY9QW0) a sub-fund of Nuveen Global Investors Fund Public Limited Company ("Nuveen GIF"), to which none of the exemptions in sections EX 29 to 43 of the Income Tax Act 2007 apply, is a type of attributing interest for which the investor may not use the fair dividend rate ("FDR") method to calculate foreign investment fund income for the interest.

Reference

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

Discussion (which does not form part of the determination)

Shares in the New Zealand Dollar ("NZD") denominated class of the Nuveen Global Sustainable Bond Fund ("the Fund"), an Irish Managed Investment Scheme, are an attributing interest in a foreign investment fund ("FIF") for New Zealand resident investors when none of the exemptions in sections EX 29 to EX 43 of the Income Tax Act 2007 apply. The Fund is a sub-fund of the Nuveen GIF and is incorporated under the laws of Ireland.

Nuveen GIF is structured as an umbrella fund with segregated liability between sub-funds. These sub-funds do not have a separate legal personality.

The Fund invests in a portfolio of international fixed interest securities (global bonds) and other financial arrangements. The Fund has on issue a number of share classes, including the NZD Hedged share class, that provides holders of that class of units with an interest in the pool of investments held by the Fund. Foreign currency hedging arrangements are in place which effectively provide investors in the NZD Hedged share class with an NZD denominated return on the financial arrangements and other investments held by the Fund.

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

Section EX 46(10)(c) of the Income Tax Act 2007 does not apply to prevent the use of the FDR method for interests in the NZD Class of the Fund given that the Fund does not have a distinct legal personality separate from Nuveen GIF. As such, the entire portfolio of Nuveen GIF is taken into consideration when examining whether the 80% test is satisfied. However, Section EX 46(10)(c) would apply to prevent the use of the FDR method if the Fund represented a separate foreign company and the NZD Class was the only class of share on issue.

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

On that basis, where a New Zealand resident invests in the NZD Class of the Fund, and hedging to NZD is undertaken by the non-resident issuer, I consider that it is appropriate for them to be excluded from using the FDR method.

Scope of determination

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

- This non-resident issuer:
 - is incorporated in Ireland and issues multiple classes of shares; and
 - is known at the date of this determination as Nuveen GIF; and
 - is structured as an umbrella fund with segregated liability between sub-funds.
- The attributing interest consists of the NZD class of share, issued in Nuveen Global Sustainable Bond Fund, a sub-fund of Nuveen GIF. This class of shares provides exposure solely to a portfolio predominantly of fixed interest securities and other financial arrangements;
- The non-resident issuer maintains a facility to hedge their interest in the NZD Class of the Fund to NZD. The facility will remove 80% to 125% of the foreign currency risk for the attributing interest and be entered with the sole purpose and net effect of offsetting exposure to the foreign currency exchange movements.

Conditions applying to this determination

It is a condition of this determination that the investment in the Fund and hedging undertaken by the non-resident issuer are part of an overall arrangement that seeks to provide the New Zealand resident investor with a return that is economically equivalent to a debt instrument denominated in New Zealand dollars.

In addition, it is a condition of this determination that an investor will not be excluded from using the FDR method to calculate FIF income from an interest where the absolute value of the Fund's investment in global fixed income securities (directly or indirectly via derivatives) plus the fair value of the related hedges plus cash and cash equivalents (together referred to as "the numerator") is 80% or less than the combined total of the numerator plus the absolute nominal value of other derivatives (together referred to as "the denominator") for a continuous period of 45 days. For the purposes of calculating the numerator and denominator hedging to NZD is excluded. Should this occur, the determination will cease to apply from the first day of the quarter immediately following the expiry of the 45-day period.

Interpretation

In this determination, unless the context otherwise requires –

"Fair dividend rate method" means the fair dividend rate method under section YA 1 of the Income Tax Act 2007;

"Financial arrangement" means financial arrangement under section EW 3 of the Income Tax Act 2007;

"Foreign investment fund" means foreign investment fund under section YA 1 of the Income Tax Act 2007;

"New Zealand resident" means a person that is resident in New Zealand for the purposes of the Income Tax Act 2007;

"Non-resident" means a person that is not resident in New Zealand for the purposes of the Income Tax Act 2007;

"The Fund" means the Nuveen Global Sustainable Bond Fund, a sub-fund of Nuveen Global Investors Fund Public Limited Company.

Determination

Subject to the conditions recorded above, an attributing interest in a FIF to which this determination applies is a type of attributing interest for which a person may not use the fair dividend rate method to calculate FIF income from the interest.

Application Date

This determination applies for the 2025-2026 income year and subsequent income years.

Under section 91AAO(3B) of the Tax Administration Act 1994, this determination does not apply for a person and an income year beginning before the date of issue unless the person chooses that the determination applies for the income year.

Dated on this 8th day of October 2025.

Iain McConville
Technical Specialist

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 25/05: Ministry of Education

Issued | Tukuna: 23 October 2025

The Arrangement is the payment of bursaries that Initial Teacher Education (ITE) providers make to eligible student teachers under the School Onsite Training Programme. To be eligible, student teachers must be hosted in schools 3 days a week while completing their 1year graduate or postgraduate ITE programme, approved by the Teaching Council, that will lead to teacher registration.

The Ministry of Education funds the bursary payments that the ITE providers make.

To the extent that a bursary payment an ITE provider makes to a student teacher under the Arrangement is income, it is exempt income of the student teacher under s CW 36 of the Income Tax Act 2007.

START DATE – END DATE | RĀ TĪMATA – RĀ MUTUNGA

1 September 2025 – 31 August 2028

Product Ruling | Whakataunga Whakaputanga – BR Prd 25/05

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

Name of person who applied for the Ruling | Ingoa o te tangata i tono i te Whakatau

This Ruling has been applied for by the Ministry of Education (the Ministry).

Taxation Laws | Ture Tāke

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

This Ruling applies in respect of s CW 36.

The Arrangement to which this Ruling applies | Te Whakaritenga i pāngia e tēnei Whakataunga

The Arrangement is the payment of bursaries that Initial Teacher Education (ITE) providers make to eligible student teachers under the School Onsite Training Programme (SOTP).

The Ministry funds the bursary payments that the ITE providers make.

The following paragraphs set out further details of the Arrangement.

Background

1. The SOTP is a government-funded initiative that the Ministry administers. It funds places in school-based ITE programmes, where teacher trainees are hosted in schools for 3 days a week while studying their Teaching Council-approved ITE programme.
2. The SOTP combines school-based experience with a full-time, 1-year ITE programme. It allows teacher trainees to study while gaining classroom experience and observing important areas of teaching like classroom management. Spending more time in school supports teacher trainees to develop confidence and capability in preparation for their first year as a beginning teacher.

3. Under the SOTP, student teachers will receive a bursary (SOTP Bursary).
4. For the 2026 intake, 465 funded bursary places will be available.
5. ITE providers apply to the Ministry for funding to provide approved SOTP Bursaries. As part of the application process, ITE providers are required to work with participating host schools.
6. To be considered for funding for the SOTP, ITE providers must have an approved 1year graduate or postgraduate ITE programme that:
 - a) will lead to teacher registration; and
 - b) is focused on primary or secondary education.
7. The following are additional requirements for ITE providers to receive funding for the SOTP Bursaries:
 - a) Providers must demonstrate that they understand work-based practice and integrate it into their programme design and delivery. This includes confirming that school partners are involved in course design and delivery and providing evidence of how the SOTP delivers differentiated wraparound support and structure for student teachers.
 - b) Providers must supply proof that their assessment includes authentic evidence generated through practice. Part of that proof must come from an onsite assessment involving mentor teachers and other school staff where appropriate.
 - c) Providers must have clear agreements with schools, addressing how appropriately experienced mentor teachers will support student teachers on site within a whole-school approach.
 - d) Primary school ITE programme providers must also demonstrate that their programme has an explicit focus on preparing teachers to teach to the new curriculum. Key focus areas include structured literacy, structured mathematics, and the science of learning and use of explicit instruction.
8. The key responsibilities of ITE providers under the SOTP are to:
 - a) market and promote their programme and SOTP-funded places;
 - b) provide programme governance;
 - c) monitor and report on the programme;
 - d) provide ongoing learning and development for student teachers;
 - e) enrol students in an approved ITE programme that leads to teacher registration;
 - f) act as a go-between for the Ministry and participating schools; and
 - g) collect data and meet the Ministry's reporting requirements.
9. Schools that host a student teacher under an ITE programme also need to meet the following requirements.

Primary schools must:

 - a) demonstrate a solid understanding of the science of learning and its application in school;
 - b) demonstrate a school-wide commitment to professional learning and development (PLD) in maths and structured literacy; and
 - c) have available an experienced mentor teacher (ie, with 4 years or more of teaching experience) who has undertaken PLD in structured literacy and structured mathematics.

Secondary schools must:

 - a) have a good understanding of the science of learning and its application in school; and
 - b) have available an experienced mentor teacher (ie, with 4 years or more of teaching experience).
10. The Ministry assesses each application from ITE providers using a weighted assessment, which is communicated to the sector. Based on this assessment, the Ministry allocates the available places to the ITE providers and schools. It then establishes contracts with selected ITE providers.
11. A list of ITE providers of approved ITE programmes leading to teacher registration through the SOTP was provided to Inland Revenue on 25 August 2025. The list includes the main universities.
12. The host school in the ITE programme may be a state or private/independent school but not a charter school.
13. The ITE provider is to pay the SOTP Bursary of \$19,930 at regular intervals to each eligible student teacher, over the course of the academic year.

14. A recipient may use the SOTP Bursary to pay fees for the ITE programme they are enrolled in, as well as to pay living costs (eg, accommodation, transport and childcare) and course-related costs (eg, materials and equipment).
15. The value of the bursaries and the number of funded places available may change in later years. However, the bursary recipients will always be subject to the eligibility criteria and terms and conditions outlined at [16]).
16. To be eligible for a SOTP Bursary, a student teacher must:
 - a) be enrolled in a 1-year graduate or postgraduate ITE programme approved by the Teaching Council that will lead to teacher registration and that is focused on primary or secondary education;
 - b) be placed in a host school for 3 days per week or equivalent (eg, 3 school days or 2 school days and 2 other mornings, depending on the needs of the ITE programme, the school and the teacher trainee). This onsite time is separate to placement requirements (see below);
 - c) meet the placement day requirements of the approved ITE programme that they are enrolled in; and
 - d) be a New Zealand citizen or New Zealand permanent resident.
17. Student teachers awarded a 2026 SOTP Bursary are not eligible to be a recipient of a TeachNZ Scholarship.
18. The Ministry provides a school contribution of \$2,000 through the ITE provider to host schools as part of the programme. The \$2,000 school contribution is made directly to the host school from the ITE provider. The student teacher does not receive it and it is not part of the SOTP Bursary.
19. The SOTP Bursary does not involve any arrangements for employment or bonding of the student teacher with the ITE provider or placement school.
20. Recipients are under no obligation to provide any services to the ITE provider or host school in return for the payment of the SOTP Bursary.
21. Applications from ITE providers for SOTP funding closed in September 2025 for the 2026 academic year.

How the Taxation Law applies to the Arrangement | Ko te pānga o te Ture Tāke ki te Whakaritenga

The Taxation Law applies to the Arrangement as follows:

- (a) To the extent a bursary payment the ITE provider makes to a student teacher under the Arrangement is income, it is exempt income of the student teacher under s CW 36.

Period or income year for which this Ruling applies | Te wā, te tau moni whiwhi rānei i pāngia ai e tēnei Whakataunga

This Ruling will apply for the period beginning on 1 September 2025 and ending on 31 August 2028.

This Ruling is signed by me on the 23rd day of October 2025.

Amy McGimpsey

Group Lead | Kaihautū ā-rōpū

Customer Compliance Services | Ratonga Kiritaki me te Tautukunga

BR Prd 25/06: Ministry of Education

Issued | Tukuna: 23 October 2025

The Arrangement is the payment of bursaries that the Ministry of Education makes to eligible student teachers under the Go Rural: Isolated Placements Fund. The bursaries are awarded to student teachers who are hosted in an isolated or rural, state or state-integrated school while completing their Initial Teacher Education programme that is Teaching Council approved.

The Ministry of Education funds the bursaries.

To the extent that a bursary payment the Ministry of Education makes to a student teacher under the Arrangement is income, it is exempt income of the student teacher under s CW 36 of the Income Tax Act 2007.

START DATE – END DATE | RĀ TĪMATA – RĀ MUTUNGA

23 October 2025 – 28 February 2029

Product Ruling | Whakataunga Whakaputanga – BR Prd 25/06

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

Name of person who applied for the Ruling | Ingoa o te tangata i tono i te Whakatau

This Ruling has been applied for by the Ministry of Education (the Ministry).

Taxation Laws | Ture Tāke

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

This Ruling applies in respect of s CW 36.

The Arrangement to which this Ruling applies | Te Whakaritenga i pāngia e tēnei Whakataunga

The Arrangement is the payment of bursaries that the Ministry makes to eligible student teachers under the Go Rural: Isolated Placements Fund (Go Rural Bursary) programme.

The Ministry funds the bursaries.

The following paragraphs set out further details of the Arrangement.

Background

1. The Go Rural Bursary is a government-funded initiative that the Ministry administers. It funds places in school-based Initial Teacher Education (ITE) programmes in rural or isolated areas. This gives student teachers the opportunity to gain experience in rural or isolated settings and build relationships with rural or isolated schools while working towards their teaching qualification.
2. Completing a school placement is an important part of a student teacher's ITE programme. Often student teachers attending placements in rural or isolated schools face greater costs than when they are placed in schools nearer their ITE provider. The Go Rural Bursary is intended to support student teachers to undertake placements at rural or isolated schools in the final year of their ITE programme.
3. The bursary is a \$4,000 lump sum payment that the Ministry makes directly to eligible student teachers.
4. The Ministry intends to implement the Go Rural Fund programme in the 2025/26 June financial year. Applications will be made available from 1 March 2026.
5. For the 2025/26 financial year, 123 funded places are available across 454 state and state-integrated schools with an isolation index of 1.27 or higher.
6. The value of the bursaries and the number of funded places available may change in later years. However, the bursary recipients will always be subject to the eligibility criteria and terms and conditions outlined at [9].
7. A student teacher can use the bursary payment to pay fees for the ITE programme they are enrolled in, as well as living costs (eg, accommodation, transport and childcare) and course-related costs (eg, materials and equipment).

8. A recipient of another bursary or scholarship that the Ministry provides may also apply for the Go Rural Bursary if they meet the eligibility criteria.
9. To be eligible for a Go Rural Bursary, an applicant must be:
 - a) enrolled in a Teaching Council-approved primary or secondary ITE programme, leading to teacher registration;
 - b) in their final year of their ITE study;
 - c) attending a placement at a state or state-integrated school with an isolation index of 1.27 or higher;
 - d) attending a placement that is at least 25 days in length; and
 - e) a New Zealand citizen or New Zealand permanent resident.
10. Recipients may be awarded a Go Rural Bursary once only.
11. The bursary does not include any arrangements for employing the student teacher with the Ministry or placement school.
12. The bursary does not include any bonding arrangements between the student teacher and the Ministry or placement school.
13. Recipients are under no obligation to provide any services to the Ministry for the payment of the bursary.

How the Taxation Law applies to the Arrangement | Ko te pānga o te Ture Tāke ki te Whakaritenga

The Taxation Law applies to the Arrangement as follows:

- (a) To the extent a bursary payment the Ministry makes to a student teacher under the Arrangement is income, it is exempt income of the student teacher under s CW 36.

Period or income year for which this Ruling applies | Te wā, te tau moni whiwhi rānei i pāngia ai e tēnei Whakataunga

This Ruling will apply for the period beginning on 23 October 2025 and ending on 28 February 2029.

This Ruling is signed by me on the 23rd day of October 2025.

Amy McGimpsey

Group Lead | Kaihautū ā-rōpū

Customer Compliance Services | Ratonga Kiritaki me te Tautukunga

INTERPRETATION STATEMENTS

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

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

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

Some interpretation statements may be accompanied by a fact sheet summarising and explaining the main points. Any fact sheet should be read alongside its corresponding interpretation statement to completely understand the guidance. Fact sheets are not binding on the Commissioner. Check taxtechnical.ird.govt.nz/publications for any fact sheets accompanying an interpretation statement.

IS 25/22: GST – Secondhand goods input tax deduction

Issued | Tukuna: 11 November 2025

This interpretation statement discusses the requirements that must be met for a registered person to claim a secondhand goods input tax deduction. This includes, among other things, a discussion of the requirement that the goods be secondhand and the meaning of secondhand. This interpretation statement also discusses exceptions and restrictions on the amount of secondhand goods input tax deduction that can be claimed, including where the supplier and the recipient are associated persons.

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

REPLACES | WHAKAKAPIA

- GST: claims for secondhand goods input tax credits on property transactions between associated persons. *Tax Information Bulletin* Vol 5, No 11 (April 1994).
- GST – the definition of secondhand goods. *Tax Information Bulletin* Vol 6, No 5 (November 1994).

Introduction | Whakataki

1. This interpretation statement discusses the requirements that must be met for a registered person to claim a secondhand goods input tax deduction for goods they acquire for their taxable activity.
2. Among other things, the discussion covers the requirement that the goods be secondhand and the meaning of secondhand. This interpretation statement also discusses exceptions and restrictions on the amount of secondhand goods input tax deduction that can be claimed, including if the supplier and the recipient are associated persons.
3. Secondhand goods input tax deductions can be claimed on the acquisition of a good only if the supply of the good is not a taxable supply. As the supply is not taxable, the supplier does not charge GST on the supply of the good. Nevertheless, the recipient can be allowed a secondhand goods input tax deduction for an imputed amount.
4. By allowing a deduction for secondhand goods in this way, the Act operates on an assumption that, despite GST not being charged on the supply in question, GST will have been incurred earlier by the supplier on their inputs, and that this GST effectively is embedded in the cost of the secondhand goods.¹

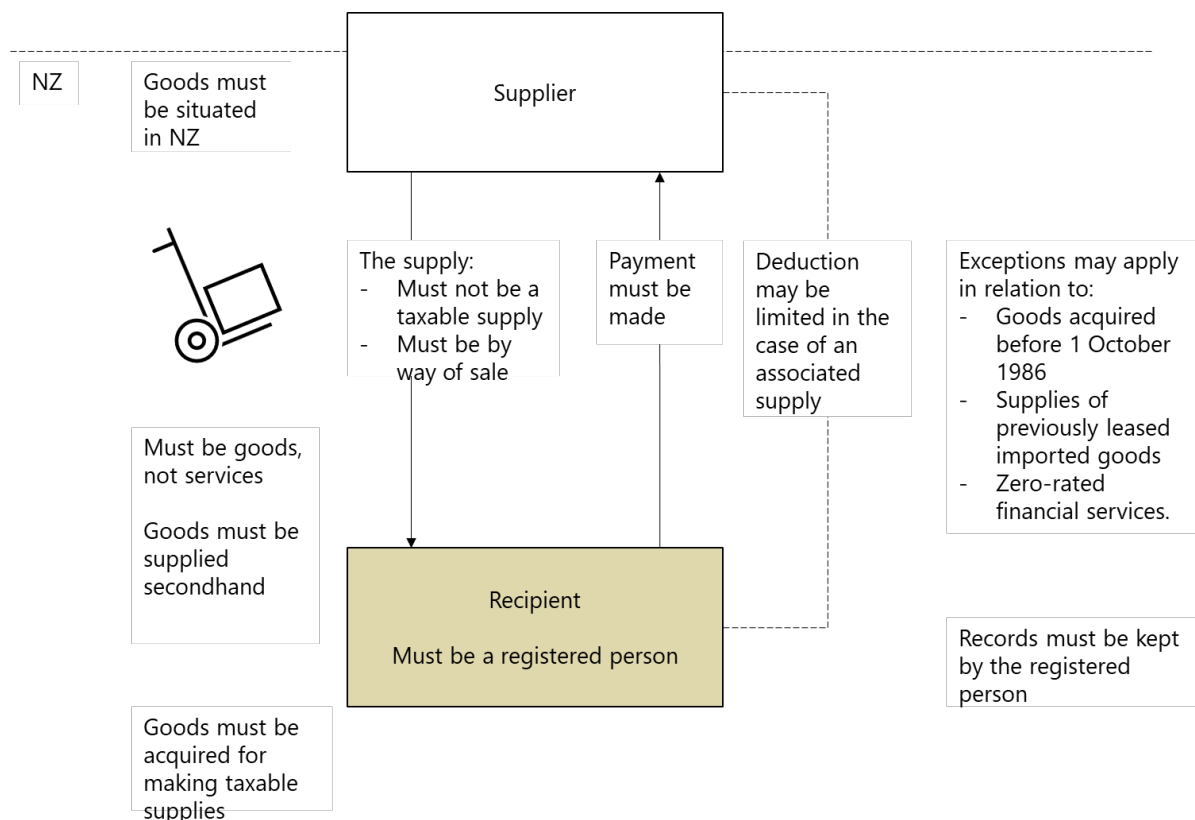
¹ *Glenharrow Holdings Ltd v CIR* [2008] NZSC 116, (2009) 24 NZTC 23,236 at [46]. This assumption will not always be true, which is why some limits on deductibility are imposed, for example, in the case of associated supplies (see from [133]).

Analysis | Tātari

Requirements for a secondhand goods input tax deduction

5. In calculating the amount of tax payable for a period, a registered person can claim deductions for input tax if certain requirements are met.²
6. There are standard input tax deduction requirements that apply to the acquisition of any goods or services (including secondhand goods) and specific requirements that apply in the case of secondhand goods.
7. The requirements are illustrated in Diagram | Hoahoa 1.

Diagram | Hoahoa 1 - Requirements



Standard input tax deduction requirements

8. Standard input tax deduction requirements include that the:
 - person claiming the input tax deduction must be a registered person (see [12]); and
 - goods or services must be acquired for making taxable supplies (see [15]).
9. This statement does not discuss these requirements in detail. This statement focusses on the secondhand goods input tax deduction requirements.

Secondhand goods input tax deduction requirements

10. Specific secondhand goods input tax deduction requirements include the following:
 - The goods acquired must be secondhand goods. See [16].
 - The supply of the goods to the person must have been by way of sale. See [83].
 - The goods must have been “situated in New Zealand” at the time of supply. See [88].
 - The supply must not have been a taxable supply. See [93].

² Sections 3A(2) and 20(3).

- A payment must have been made for the supply. A secondhand goods input tax deduction for a taxable period is allowed only to the extent that a payment has been made during that taxable period³ for the supply. See [106].
 - Certain records must be kept of the supplies received.⁴ See [110].
11. Exceptions, which prevent a secondhand goods input tax deduction, apply in relation to:
- goods acquired before 1 October 1986 (see [112]);
 - supplies of previously-leased imported goods (see [114]); and
 - zero-rated financial services (see [117]).

The person claiming the input tax deduction must be a registered person

12. To claim an input tax deduction, the person claiming the input tax deduction must be a registered person.⁵
13. A person may be liable to be a registered person or they may voluntarily register. In either case, to be a registered person, a person must either be carrying on a taxable activity or intend to carry on a taxable activity.⁶
14. For guidance on whether a taxable activity exists, see **IS 25/21: GST – taxable activity**.⁷

Acquired for making taxable supplies

15. To claim an input tax deduction for the acquisition of goods or services, the goods or services must:
- be used for, or be intended to be used in, making taxable supplies;⁸ or
 - have been acquired for the principal purpose of making taxable supplies if s 20(3CC) applies (this can apply in relation to goods or services acquired for \$10,000 or less (excluding GST)).⁹

Secondhand goods

16. The term “secondhand goods” is defined,¹⁰ but the definition contains only exclusions (discussed below).
17. Therefore, the term must be interpreted based on the meaning of the two words. For a secondhand good to exist, there must be a supply of goods, as defined in the Act, and the goods must be secondhand.¹¹ The meaning of goods and secondhand are discussed below.

Goods

18. A secondhand goods input tax deduction is only available in relation to a supply of goods, not services.
19. “Goods” is defined in s 2:
- goods** means all kinds of personal or real property; but does not include choses in action, money, cryptocurrency, or a product that is transmitted by means of a wire, cable, radio, optical or other electromagnetic system or by means of a similar technical system
20. “Real property” is a legal term used to describe land and things growing in or attached to the land, or rights over the land.¹² Therefore, land is a good for the purposes of the Act. Land includes specific interests or rights in land; for example, a forestry right.
21. “Personal property” is property that is not classified as real property. It includes movable items.

3 Or during the relevant earlier period if a deduction is made in accordance with the proviso in s 20(3).

4 Section 19H prescribes record-keeping requirements for secondhand goods input tax deductions.

5 In s 3A input tax is defined “in relation to a registered person”. Further, s 20, which discusses the calculation of tax payable, allows a “registered person” to deduct tax.

6 Section 51.

7 IS 25/21: GST – taxable activity *Tax Information Bulletin* Vol 37, No 10 (November 2025): 10.

8 Under s 20(3C)(a), a deduction is allowed only to the extent to which the goods or services are used for, or are intended to be used in, making taxable supplies.

9 Section 20(3CB) and (3CC).

10 Section 2.

11 In *Case V9* (2001) 20 NZTC 10,101 at [198], the Taxation Review Authority described the term as a composite one.

12 *Dictionary of New Zealand Law* (LexisNexis).

22. "Goods" does not include money. Among other things, "money" includes bank notes and coins, but an exception is made for a collector's piece, investment article or item of numismatic interest. This means, for example, that a supply of a collectible coin is a supply of goods.
23. "Goods" does not include choses in action. A chose in action is an intangible right that has no existence apart from the recognition given by the law or that confers no present possession of a tangible object. For example, the right to recover a debt is a chose in action.
24. Although not common, some things are treated as being neither real nor personal property, so are excluded from the definition of goods. For example, as discussed in **BR Pub 15/01 and BR Pub 15/02: Secondhand goods input tax deductions – fishing quota, coastal permits and certificates of compliance**,¹³ under s 122 of the Resource Management Act 1991, coastal permits and certificates of compliance (types of resource consent) are deemed not to be "personal or real property". This means coastal permits or certificates of compliance are not "goods", so cannot be supplied as secondhand goods.

Secondhand

The Commissioner's view

25. The Commissioner's view of the meaning of secondhand is as follows:
 - The concept of secondhand is flexible.
 - Under the ordinary meaning, a good is secondhand when acquired if it is not acquired from the original source (in other words, if it has been previously owned) or has been previously used.
 - Case law has held that a good is secondhand if it has been used or treated or stored by a previous owner in such a manner that it can no longer be regarded as new.
 - "Use" in this context means being used for the good's intrinsic purpose as opposed to being used as trading stock, for example.
 - If a good is acquired from the producer of the good, the good will not be secondhand unless the producer has used, or intended to use, the goods themselves (use as trading stock does not count). This is because the producer is the original source.
 - A good is not secondhand merely because it has passed from the producer through the hands of a wholesaler, distributor or retailer of the good, unless one of these persons acquired the good to use themselves (again, use as trading stock does not count). It would be unnatural to describe a good being supplied through such a person as being supplied by the person secondhand.
 - A good that has not been used, will nevertheless be secondhand when supplied by a person if the person produced or acquired the good intending to use the good themselves (as opposed to producing or acquiring the good as trading stock, for example). In this case, a good can be secondhand even if the person has not used the good. As noted above, the concept of secondhand is flexible and a good is secondhand if it has been used or treated or stored by a previous owner in such a manner that it can no longer be regarded as new. If they actually use the good, it is secondhand on that basis as well. This is illustrated in Example | Tauira 1 and Diagram | Hoahoa 2.
26. To be clear, the Commissioner is not suggesting that trading stock cannot be a secondhand good. The Commissioner's view is that a good is not secondhand when supplied by a producer or when supplied through an initial distribution network (where the good will be trading stock), before being supplied to the first person who uses or intends to use the goods themselves. A used good forming the trading stock of a secondhand store, for example, will generally be secondhand goods. Land held for resale will also generally be secondhand (see from [52]).
27. It is acknowledged that in some cases, it may be difficult for a purchaser to determine whether the supplier acquired a good to use themselves. Relevant factors to consider could vary depending on the facts, but generally regard should be had to evidence of the supplier's activity and the nature and circumstances of the supply. For example, if the supplier has a history of making such supplies, this could suggest they did not acquire the good to use themselves.

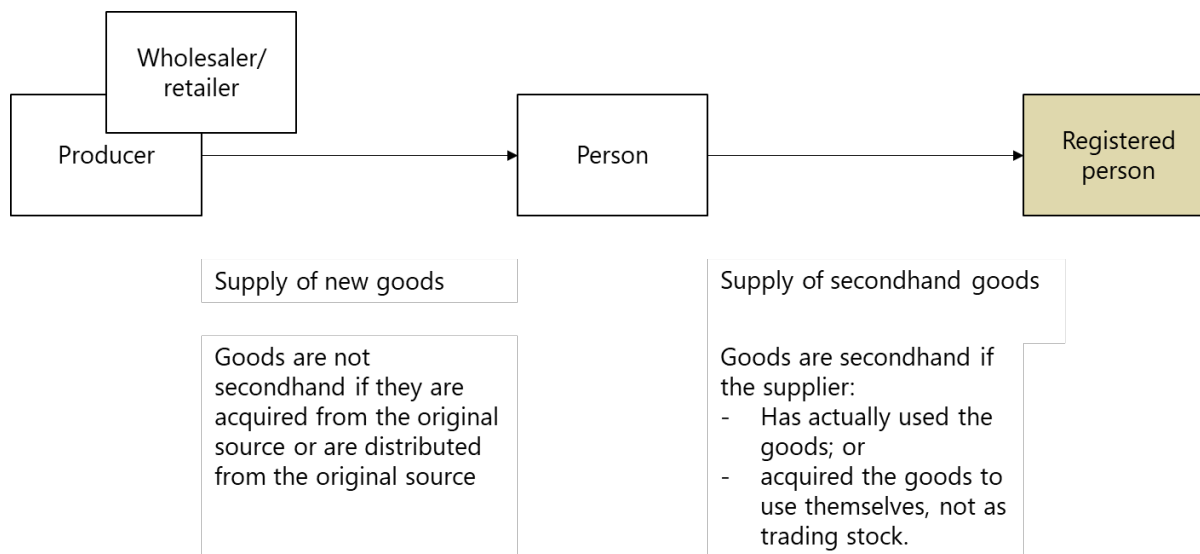
¹³ BR Pub 15/01 and BR Pub 15/02: Secondhand goods input tax deductions – fishing quota, coastal permits and certificates of compliance *Tax Information Bulletin* Vol 27, No 2 (March 2015): 3.

Example | Tauira 1 – Meaning of secondhand

ABC Wines recently ceased its GST registration. Before it ceased its registration, ABC Wines purchased a new bottling machine. The machine is still in its shipping container and hasn't been used. On cessation, ABC Wines was deemed to make a supply of all its assets, including the bottling machine.

Subsequently, as an unregistered person, ABC Wines sells the bottling machine to another wine maker, XYZ Wines.

XYZ Wines is able to claim a secondhand goods input tax deduction. The machine is secondhand because of ABC's previous ownership. Previous ownership is relevant here because ABC acquired the machine to use itself.

Diagram | Hoahoa 2 - Supply of secondhand goods

28. The reasons for the Commissioner's view are discussed below.

Ordinary meaning

29. The *Oxford English Dictionary* defines the adjective "secondhand" as "Not original or obtained from the original source" or "not new, having been previously used or worn by another".¹⁴

Case law

30. One of the key cases on the meaning of secondhand is *Case N16*.¹⁵ Comments in this case can be taken out of context, so it is helpful to discuss the case in some detail below.

31. In *Case N16*, the Taxation Review Authority (TRA) was required to determine whether deer velvet purchased from an unregistered person was secondhand goods. The TRA concluded that the deer velvet was not a secondhand good when supplied by farmers or hunters to the wholesalers. The TRA stated from 3,147:

In this case, a farmer or a hunter has obtained the deer antlers (when in velvet) of young deer and sliced them up and frozen them. I understand that they were then parcelled as one would parcel meat. Then these people called "commission buyers" acquire the product from the farmer, or the hunter, and deliver it to the exporter or wholesaler, - in this case, the objector. At that point it is possible to regard the product, due to the way it has by then been handled, as secondhand, but I would regard this as an unnatural interpretation. The word "secondhand" as an adjective to "good" or "goods" means, in my view, that in some way or another the item has been used or treated or stored by a previous owner in such a manner that it can no longer be regarded as new. Items in a retail shop are regarded as new, but they have quite possibly passed through a number of hands prior to being available at retail. Items in the shop of a secondhand dealer are regarded as secondhand, because they have been used for their intrinsic purpose by at least one prior owner; and even items which are in new condition will then be regarded as secondhand.

¹⁴ The *Oxford English Dictionary* (online, accessed on 19 June 2025) defines the adjective "secondhand" as "Not original or obtained from the original source" or "Not new, having been previously used or worn by another". See also *Case N16* (1991) 13 NZTC 3,142 (TRA) at 3,147.

¹⁵ *Case N16* (1991) 13 NZTC 3,142 (TRA).

In my view, primary produce is not normally referred to as secondhand because its use is that of consumption. Nevertheless, it may be appropriate to refer to produce or manufactured food items as secondhand in certain contexts, possibly for instance, at some type of clearance sale on behalf of a liquidator or receiver, or after a fire. However, generally speaking, I take the view that primary produce, such as deer velvet, is not being sold on a secondhand goods basis when it is acquired by a distributor or exporter from a farmer or hunter, whether or not through the use of a commission agent.

I agree with counsel that the concept of secondhand relates to pre-ownership or pre-use. I agree with Mr Brownie that the emphasis is on pre-use. I consider that there is quite some commonsense flexibility in ascertaining whether a good is still new or has become secondhand. I do not regard second ownership as necessarily rendering an item secondhand. Many goods pass from manufacturer to wholesaler to retailer to customer or consumer (with other levels of distributors sometimes also involved), and yet are not regarded as secondhand at the consumer purchase level, even though the item has been used as stock-in-trade at the various distribution levels. The good is not usually regarded as secondhand until it has been used for its intrinsic purpose. The concept of secondhand is inappropriate to produce, because use of produce is usually by human consumption whereafter the good is no longer in existence. Deer velvet is desired by some people for consumption. Indeed, it is consumed for desire.

32. The TRA stated that:

- The concept of secondhand is flexible.
- A good is secondhand if it has been used or treated or stored by a previous owner in such a manner that it can no longer be regarded as new.
- The concept of secondhand relates to pre-ownership or pre-use.
- The emphasis is on pre-use. This does not mean that pre-ownership is irrelevant.
- Pre-ownership (or second ownership) does not necessarily cause an item to be secondhand. Again, this does not mean that pre-ownership is irrelevant.
- A good is not usually regarded as secondhand until it has been used for its intrinsic purpose.
- The concept of secondhand is inappropriate for produce, because produce is usually used through human consumption, after which the good no longer exists.
- It may be appropriate to refer to produce or manufactured food items as secondhand in certain contexts, possibly for instance, at some type of clearance sale on behalf of a liquidator or receiver, or after a fire.

33. The TRA's comments about pre-ownership not causing a good to be secondhand were made in the context of the pre-ownership of the goods by the farmers and hunters. This is consistent with the TRA's suggestion that, when the deer velvet was sold to the wholesalers, it would be an unnatural interpretation to regard the good as being secondhand. It is also consistent with the TRA's comments that items in a retail shop are regarded as new, notwithstanding that they have possibly passed through a number of hands prior to being available at retail. In the Commissioner's view, if the goods are supplied to, or produced by, a person who intends to use the goods themselves, the goods may be secondhand if subsequently supplied by the person. This is illustrated in Example | Tauira 1.
34. The TRA also stated that the emphasis is on pre-use and that a good is not usually regarded as secondhand until it has been used for its intrinsic purpose. In the Commissioner's view, the TRA was not suggesting a good would need to actually be used for it to be secondhand. The TRA made the statement that the emphasis is on pre-use in the context of a preceding comment on the use of goods as trading stock in the various distribution levels.
35. In the Commissioner's view, a good that has not been used will nevertheless be secondhand when supplied by a person if the person produced or acquired the good intending to use the good themselves (as opposed to producing or acquiring the good as trading stock). In this case, an unused good can be secondhand on the basis of the person's ownership. As noted above, the concept of secondhand is flexible and a good is secondhand if it has been used or treated or stored by a previous owner in such a manner that it can no longer be regarded as new. If they actually use the good, it is secondhand on that basis as well.
36. The TRA's comment on primary produce is discussed later at [57].
37. Another case that considered the meaning of secondhand goods is *LR McLean*.¹⁶ In *LR McLean*, the Court of Appeal considered whether wool merchants were allowed a secondhand goods input tax deduction for wool purchased from unregistered suppliers.

16 *LR McLean & Co Ltd v CIR* (1994) 16 NZTC 11,211 (CA). See also *Case T28* (1997) 18 NZTC 8,197 (TRA).

38. The facts in *LR McLean* and *Case N16* are similar in that both involved the supply of goods from producers. As noted above, it would be an unnatural interpretation of the word secondhand, to describe a supply of goods from a producer (an original source) as a supply of secondhand goods.
39. However, *LR McLean* is notable for a purpose argument made by the taxpayers and the Court of Appeal's reaction to the argument. In *LR McLean*, the taxpayers argued that to accord with the scheme and purpose of the legislation the expression "secondhand good" must be given the meaning of any goods that have been purchased by a registered person (whether they fall within the ordinary meaning of secondhand or not). The crux of the taxpayer's argument was that the GST regime and, in particular, the input tax credit mechanism, is designed to ensure double tax is not assessed on the same added value.
40. The Court of Appeal agreed that in general the GST regime ties the tax liability of a registered person to the value added by the person and that the input tax mechanism in the Act generally ensures tax neutrality. However, the court stated that it cannot be said that the statutory scheme does not provide cases of double tax liability. The court referred to the example of a supply of services by an unregistered person to a registered person, which also does not qualify for input tax and can result in double tax. The court stated that crucially Parliament chose the concept of secondhand goods as the yardstick for allowing input tax deductions. The court noted that Parliament could have used "goods" without the qualifying adjective "secondhand" in para (c) of the definition of input tax, which would have ensured the tax neutrality of purchase transactions by registered persons liable for GST. However, Parliament elected not to do so. Therefore, the term must be given appropriate meaning.
41. The meaning of secondhand is illustrated in Example | Taurira 1.

Impact on previous guidance

42. This draft interpretation of secondhand is different in some respects from previous guidance in:
- **Question we've been asked: Funeral expenses paid by funeral directors in connection with funeral arrangements;**¹⁷
 - **BR Pub 07/01: Forestry rights — secondhand goods GST input tax deduction;**¹⁸
 - **BR Pub 15/01 and BR Pub 15/02: Secondhand goods input tax deductions – fishing quota, coastal permits and certificates of compliance.**¹⁹

Funeral expenses – flowers purchased from unregistered suppliers

43. With respect to the question we've been asked in relation to funeral expenses, it is important to note that normally funeral directors act as agents for their customers (meaning the customers are treated as acquiring any goods), so the issue of whether flowers are secondhand goods does not arise. Nevertheless, it was stated in the guidance that:
- Even if funeral directors acquired services as principals, input tax credits are not allowable on services supplied by non-registered persons. An input tax credit may be allowable on the sale of "secondhand goods" by non-registered persons to funeral directors as principals. **"Secondhand goods" are goods which have been previously owned and used for their intrinsic purpose by a previous owner: Case N16 (1991) 13 NZTC 3,142; L R McLean & Co Ltd v CIR (1994) 16 NZTC 11,211.** For example, **flowers would not be "secondhand goods" for GST purposes since their previous use for their intrinsic purpose would normally result in their no longer being regarded as new.** Therefore, an input tax credit would not be allowable to funeral directors on flowers acquired from a non-registered person, whether acquired by funeral directors as a principal or agent. [Emphasis added]
44. The Commissioner's position in relation to this scenario has not changed, but it could be better described as follows. Flowers will not normally be supplied secondhand because they will normally be acquired from the producer, either direct or through a distribution chain. Also, a person who acquires the flowers to use themselves (rather than as trading stock) will normally not resell the flowers. Normally, the flowers will be used once before being discarded or donated.

¹⁷ Questions we've been asked: Funeral expenses paid by funeral directors in connection with funeral arrangements *Tax Information Bulletin* Vol 13, No 8 (August 2001): 9.

¹⁸ BR Pub 07/01: Forestry rights – secondhand goods GST input tax deduction *Tax Information Bulletin* Vol 19, No 3 (April 2007): 4.

¹⁹ BR Pub 15/01 and BR Pub 15/02: Secondhand goods input tax deductions – fishing quota, coastal permits and certificates of compliance *Tax Information Bulletin* Vol 27, No 2 (March 2015): 3.

Forestry rights

45. In BR Pub 07/01, it was held that the supply of a forestry right could be a supply of secondhand goods as long as the previous owner has used the forestry right for its intrinsic purpose, namely has exercised some of the rights provided by the forestry right, for example, by establishing, maintaining, or harvesting trees.
46. There is a slight change in the Commissioner's position on this point. Based on the interpretation of secondhand discussed above, when a forestry right is first created and supplied by the creator (person A) to a recipient (person B) (without being used by the creator), the forestry right would not be secondhand because the forestry right would be supplied by the creator of the forestry right (the original source). However, assuming person B acquired the forestry right to use themselves, a subsequent supply of a forestry right (by person B) could be a supply of a secondhand good (based on person B's previous ownership of the forestry right). For the forestry right to be secondhand, person B would not need to exercise any of the rights provided by the forestry right, for example, by establishing, maintaining or harvesting the trees, (although if they have, then the forestry right would be secondhand on the basis of both their previous use and previous ownership). However, again, this assumes person B acquired the forestry right to use themselves.

Fishing quota, coastal permits and certificates of compliance

47. The interpretative position in this statement also differs from some comments made in the commentary to BR Pub 15/01 and 02. We would now express things differently. However, this does not have any effect on the application of the rulings in BR Pub 15/01 and 02 because the rulings did not turn on whether the relevant supplies were of secondhand goods.
48. In the commentary to BR Pub 15/01 and 02, *Case N16* and *LR McLean* were discussed. In relation to *Case N16*, the commentary stated:

Judge Barber considered that previous ownership of goods is not in itself necessarily sufficient to meet the test of secondhand in the GSTA. **Usually, a previous owner must have also used the goods for their intrinsic purpose.** [Emphasis added]

49. In relation to *LR McLean*, the commentary stated:

The judgments of the Court of Appeal state that the term "secondhand" should be given its ordinary or normal meaning. While "secondhand" can mean pre-owned or pre-used, **the Court concluded that it is not sufficient that the goods were previously owned.** If an item were "secondhand" simply through being previously owned, the term "secondhand" would be deprived of any practical meaning according to Richardson J. Therefore, the Court of Appeal concluded that the more relevant factor is whether the goods have been previously used.

The effect of this is that **the courts have not extended the meaning of the term "secondhand goods" to goods that have been previously owned but not previously used** for their intrinsic purpose. [Emphasis added]

50. The commentary arguably creates an impression that a good cannot be secondhand on the basis of previous ownership. However, neither *Case N16* nor *LR McLean* held that a good could not be secondhand on the basis of previous ownership. For example, in *LR McLean* the Court of Appeal stated that:

Although the term can be used of goods that have been previously owned even if not used, prior ownership does **not always** have the effect of making goods "secondhand". The ordinary meaning of the term is accurately summarised in the passage cited from Barber DJ in *Case N16*, and the construction which he adopted is that approved by Greig J in the present case. No one using the term "secondhand" in its ordinary meaning would apply it to wool sold to a merchant in the circumstances of the sales which are the subject of these proceedings. [Emphasis added]

51. The courts have applied the ordinary meaning of secondhand, which includes something that is previously owned or previously used. Some previous ownership (including the previous ownership of a producer, wholesaler, distributor or retailer) could be disregarded under the ordinary meaning, but this does not mean that previous ownership is never relevant. Goods that have never been used can be secondhand under the ordinary meaning based on previous ownership, for example, if a person buys a good to use in their taxable activity, but their plans change, and they instead sell the good.

Land can be a secondhand good

52. In case law, it appears to be accepted that land can be a secondhand good.²⁰ Land, being real property, is a good. Further, most land will have been previously used. Even if the land is vacant and hasn't been used for anything by a supplier, at some point in the past before the supplier acquired the land, it is likely to have been used for something.
53. However, it is possible to create new legal interests in land from existing legal interests. For example, an area of land can be subdivided into smaller areas, or a forestry right could be granted from an existing interest in land.
54. In the case of a simple subdivision, it might be argued that the new legal interests in land, created from the subdivision, are different from the interests in the original property. These new legal interests in land would, at least at first, not be previously used and would be supplied from an original source. From this, it might be argued that the new interests in land are not secondhand when they are first supplied. However, stepping back and considering the ordinary meaning of secondhand in the context of land, few people would describe an area of land that has recently been subdivided from a larger area as being new or unused land, merely because new legal interests have been created. This may be because, with a simple subdivision, the legal rights in the land are largely the same with the only significant difference being the areas of land to which the rights relate. Therefore, in the case of a simple subdivision, a newly subdivided lot can still be regarded as secondhand. This is illustrated in Example | Tauira 2.

Example | Tauira 2 – Simple subdivision of land

An unregistered person owns a house with a large section.

The unregistered person subdivides the property creating a front section with the house and a rear section of bare land.

The person then immediately sells the rear section to a registered person, who sometime later (on a change in use of the land – see [159]) uses the section for making taxable supplies in a home business.

The registered person may be able to claim a secondhand goods input tax deduction. Under the ordinary meaning of secondhand, most people would still regard the land as secondhand when it was acquired despite the creation of a new legal title for the land.

55. In contrast, in the case of a more specific right in land, it is arguable that something new is created – something that cannot be described as secondhand. It is considered that a forestry right (when first supplied) is an example of this (see [45]).
56. If there is a new interest in land (for example, a forestry right), the general approach discussed at [25] applies.

Primary produce is generally not secondhand

57. A supply of primary produce, such as fruit, vegetables, eggs or honey, is generally not a supply of secondhand goods.
58. In *Case N16*,²¹ the TRA stated that the concept of secondhand is inappropriate for produce, because produce is usually used through human consumption, after which the good no longer exists.
59. In the Commissioner's view, produce will normally be supplied by the producer, either directly or via a distribution chain, so the goods will not normally be secondhand based on pre-ownership. Once acquired by a person who intends to use the goods themselves, as noted by the TRA, the goods will normally be consumed and cease to exist. They will not normally be supplied again, or at least not in the same form.
60. In *Case N16*, the TRA also stated it may be appropriate to refer to produce or manufactured food items as secondhand in certain contexts, possibly for instance, at some type of clearance sale on behalf of a liquidator or receiver, or after a fire.
61. This was an *obiter dictum* comment by the TRA (which means it is not binding), and it is difficult to reconcile with the ordinary meaning of secondhand. In the Commissioner's view, goods would not be secondhand merely because they are sold on behalf of a liquidator or receiver, or after a fire. This is because the source of the goods is unchanged, and there is no change in terms of whether the goods are used.

20 That land can be a secondhand good was accepted in *Case L108* (1989) 11 NZTC 1,608 (TRA) and *Case N13* (1991) 13 NZTC 3,105 (TRA). Some doubt was expressed in *LR McLean and King v Bennetts* (1994) 16 NZTC 11,370 (CA), but in *CIR v Coveney* (1995) 17 NZTC 12,193 (CA), Richardson J appeared to accept that the resale of land is a sale of a secondhand good.

21 Discussed at [30].

62. Similarly, a supply of the fleece or wool of an animal is generally not a supply of secondhand goods because it will normally be supplied by the producer, either direct or through a distribution chain, and these goods are normally used once before being consumed or transformed into new goods (for example, by being cleaned, carded and spun into yarn).
63. A supply of some plant materials, for example flowers²² or firewood, is generally not a supply of secondhand goods for similar reasons.
64. This is illustrated in Example | Taura 3.

Example | Taura 3 - Primary produce is generally not secondhand

Zaid has a small rural property with a row of exotic trees he would like to replace with native planting. Zaid cuts the trees cut down and sell them to a firewood company.

Zaid also has some timber that he purchased that he was going to use to build a shed, but he changed his mind and instead sold the timber to a secondhand building materials company.

Zaid is not registered for GST.

The felled trees are not secondhand as Zaid is the original source of the trees, and the felled trees have never been used. Therefore, the firewood company is not able to claim a secondhand goods input tax deduction for the felled trees.

The timber is secondhand on the basis of Zaid's previous ownership. Therefore, the secondhand building materials company can claim a secondhand goods input tax deduction.

Collectibles

65. It is considered that a supply of collectibles (for example, coins, stamps, vintage toys, trading cards or comic books) can be a supply of secondhand goods based on previous ownership or previous use. As noted at [22], a collectible coin is not included in the definition of money, so is not excluded from the definition of "good".
66. As discussed at [25], a good is secondhand when supplied by a person if the person produced or acquired the good intending to use the good themselves (as opposed to producing or acquiring the good as trading stock). In this case, a good can be secondhand even if the person has not used the good. As noted above, the concept of secondhand is flexible and a good is secondhand if it has been used or treated or stored by a previous owner in such a manner that it can no longer be regarded as new. If the person actually uses the good, it is secondhand on that basis as well.
67. Collectables will not be secondhand when supplied by a producer. They also will not be secondhand if supplied from a producer through other persons in a distribution chain.
68. When supplied by a collector, a collectible will generally be supplied secondhand because:
- the collector is not the original source;
 - collectors generally acquire collectibles for themselves or as a long-term investment, not as trading stock; and
 - even if a collector does not use a collectible (for example, if a good is simply purchased and displayed or stored in its original packaging), the collector's ownership generally means that the collectible can no longer be regarded as new.
69. This is illustrated in Example | Taura 4.

Example | Taura 4 – Collectibles may be secondhand goods

Sarah has a collection of Beanie Babies purchased between 1994 and 1999. They are all in their original packaging and are in good condition. In 2025, Sarah, who is not GST registered, sells her collection to an antique dealer, who is registered for GST, for \$2,000.

The Beanie Babies are supplied as secondhand goods based on Sarah's previous ownership of the Beanie Babies. Previous ownership is relevant in this case because Sarah acquired the items for herself (to hold as collectible items), rather than as trading stock.

Therefore, the antique dealer can claim a secondhand goods input tax deduction for the Beanie Babies.

²² See Questions we've been asked: Funeral expenses paid by funeral directors in connection with funeral arrangements *Tax Information Bulletin* Vol 13, No 8 (August 2001): 9. See also [43], the Commissioner's position in relation to this scenario has not changed, but it is better described in this statement.

Newly made goods

70. Newly made goods are not secondhand because they have not been previously used. This is illustrated in Example | Tauira 5.

Example | Tauira 5 – Newly made goods

Jamie makes jam that she sells to a gift shop. Jamie is not registered for GST.

The gift shop is not able to claim a secondhand goods input tax deduction for the jam purchased from Jamie. This is because the jam is a newly made good purchased from an original source and the jam has never been used before, so is not secondhand.

New goods created from old

71. If a good is materially altered, it can become a new good – one that is recognised as having a separate existence for GST purposes.²³ The new good created in this way is not secondhand because it is a distinct good that has not been previously used. This is illustrated in Example | Tauira 6. See also Example | Tauira 3.

Example | Tauira 6 – New goods created from old

Howard, who is not registered for GST, salvages used wine barrels from a winemaker friend. Howard cuts the barrels in half, drills drainage holds and sands the cut edges. He then sells what he has made to his local garden centre as planter boxes.

Howard has materially altered the wine barrels and has created new goods (planter boxes) that have a separate existence for GST purposes. Because the planter boxes have not been previously used, they are not secondhand. Therefore, the garden centre is not able to claim a secondhand goods input tax deduction.

Goods used overseas but not in New Zealand can be secondhand

72. Goods that have been used overseas but not in New Zealand, can be secondhand for the purposes of the secondhand goods input tax deduction.²⁴ No distinction is made in this context between goods used in New Zealand or overseas. This is illustrated in Example | Tauira 7.

Example | Tauira 7 – Sale of imported used bike

Daniele (who is not registered for GST), impulse purchases a used motor bike from an overseas seller for \$10,000 and has the bike imported into New Zealand. With freight charges of \$1,600, Daniele ends up paying \$11,600 in total plus incurs GST on importation of \$1,740.

However, after making the purchase, Daniele realises that she can't really afford the bike.

Luckily, one of her friends runs a motorcycle dealership and agrees to purchase the bike from Daniele for \$10,000. Daniele arranges for the bike to be delivered to the motorcycle dealership once it is imported into the country.

In this case, the motorcycle dealer can, assuming other requirements are met, claim a secondhand goods input tax deduction of \$1,304.35 ($\$10,000 \times 3/23$). The fact that the bike has never been used in New Zealand does not prevent a deduction.

²³ Case 4/2013 [2013] NZTRA 04; (2013) 26 NZTC 2,003 (TRA).

²⁴ In case comparisons are drawn, this differs from a requirement of the income tax Investment Boost rule, which allows a 20% upfront deduction for depreciable property if it is new or new to New Zealand.

Goods excluded from definition of secondhand goods

73. “Secondhand goods” is defined in s 2 to exclude certain goods:

secondhand goods, does not include—

- (a) secondhand goods consisting of any fine metal; or
- (b) secondhand goods which are—
 - (i) manufactured or made from, or to the extent to which they are manufactured or made from, gold, silver, platinum, or other substance, that would be fine metal if it were of the required fineness; and
 - (ii) of a kind not manufactured for sale to the public; or
- (c) livestock

Fine metal

74. “Secondhand goods” does not include secondhand goods consisting of any “fine metal”. Fine metal is defined and includes:

- gold of a fineness of not less than 99.5%;
- silver of a fineness of not less than 99.9%; and
- platinum of a fineness of not less than 99%.

75. Fine metal is excluded because a subsequent supply of these goods would be either exempt from GST or zero-rated.²⁵

76. “Secondhand goods” also does not include goods to the extent that they are composed of gold, silver or platinum and the goods are of a kind not manufactured for sale to the public, for example an alloy of lesser fineness. These goods are excluded from the definition of secondhand goods to protect the integrity of the fine metal exclusion. This is illustrated in Example | Taura 8.

Example | Taura 8 – Fine metal exclusion

Loki has a quantity of fine metal (gold) that he supplies to an unregistered person for \$10,000. No GST is charged because a supply of fine metal is an exempt supply.

The unregistered person melts the gold down and creates an alloy of gold and zinc comprising 98% gold (which is no longer fine gold). The unregistered person then sells the alloy back to Loki for \$10,000.

Loki tries to claim a secondhand goods input tax deduction of \$1,304.35 on the full cost of the alloy. However, Loki’s claim is largely disallowed. Loki’s allowable secondhand goods input tax deduction is limited to \$26.09 – being the imputed GST on the \$200 non-gold portion of the alloy.

77. Goods manufactured or made of gold, silver or platinum and of a kind manufactured for sale to the public are not excluded. This means jewellery, for example, can be a secondhand good. Supplies of these types of goods present a lower risk to the integrity of the fine metal exclusion.²⁶ This is illustrated in Example | Taura 9.

Example | Taura 9 – Jewellery can be a secondhand good

A jewellery store buys used jewellery from customers. These purchases are not taxable supplies if, for example, the customers are not GST registered or if the supplies are of personal items that are not made in the course or furtherance of a taxable activity.

The jewellery store buys an 18-karat wedding band from a non-registered customer for \$250 to on-sell. The jewellery store can claim a secondhand goods input tax deduction of \$32.61 ($\$250 \times 3/23 = \32.61) on this purchase.

²⁵ A supply of fine metal will be either an exempt supply under s 14(1)(e) or zero-rated under s 11 in the case of the first supply of newly refined fine metal.

²⁶ New Legislation *Tax Information Bulletin* Vol 29, No 5 (June 2017): 30 at 78.

Livestock

78. "Livestock" is not defined in the Act.
79. The ordinary meaning of livestock is domestic animals kept on a farm for use or profit.
80. However, case law suggests livestock can include all live animals, including for example fowl, bees and fish, if they formed part of the assets of a business.
81. The livestock exclusion was enacted as an integrity measure as some taxpayers were claiming a secondhand goods input tax deduction for the offspring of their existing livestock. It was difficult for the Commissioner to distinguish between offspring and livestock acquired from other people. Therefore, all livestock was excluded.
82. Examples of livestock in New Zealand could include (this is not an exhaustive list) sheep; goats; pigs; cattle; deer; chickens and other poultry; emus and ostriches; alpacas and llamas; horses, including horses that are kept for the purposes of racing or breeding (bloodstock); bees; working dogs; and pets purchased for resale.

Supply by way of sale

83. For a person to claim a secondhand goods input tax deduction on the supply of goods to them, the supply must have been by way of sale.
84. The purpose of this requirement is not entirely clear, but commentary released after this requirement was enacted in 1989 indicates that the amendment was intended to exclude supplies by way of lease or distribution.²⁷
85. Other supplies that may not be made by way of sale include a transfer of property to an administrator or executor on the death of a person and subsequent distributions from the administrator or executor to beneficiaries, certain trust distributions and resettlements, and certain transfers pursuant to a relationship property agreement. These supplies might be excluded from being supplies of secondhand goods for other reasons as well, for example, because the supplies do not involve consideration.
86. A compulsory acquisition can be a supply by way of sale. See **QB 13/03**: Goods and services tax – whether a compulsory acquisition of land is a "supply by way of sale".²⁸
87. This requirement is illustrated in Example | Tauira 10 and Example | Tauira 11.

Example | Tauira 10 – No secondhand goods input tax deduction for supply by way of lease

A GST registered farmer leases 20 hectares of land from their neighbour who is not registered for GST. The farmer uses this land for additional grazing in their farming business.

Land is a good and, therefore, could be a secondhand good. However, the farmer is not allowed a secondhand goods input tax deduction because the land is not supplied by way of sale.

27 Part III: Goods and Services Tax Amendment Act 1989 *Public Information Bulletin* Vol 181 (June 1989).

28 QB 13/03: Goods and services tax – whether a compulsory acquisition of land is a "supply by way of sale" *Tax Information Bulletin* Vol 25, No 7 (August 2013): 97.

Example | Tauira 11 - No secondhand goods input tax deduction for transfers to or from deceased's estate

Graeme owned a small area of land with a workshop that he used for doing up cars and other hobbies. Graeme was not registered for GST.

Graeme has recently died, and ownership of the workshop property passed to the executor of his estate before being distributed by the executor to one of Graeme's children. Graeme's child, who is registered for GST, intends to use the property for making taxable supplies.

The transfer of ownership to Graeme's estate is not a supply by way of sale, so the estate cannot claim a secondhand goods input tax deduction.

The distribution of the property to Graeme's child is also not a supply by way of sale, so Graeme's child is also not able to claim a secondhand goods input tax deduction.

It is also noted that for GST purposes, the transfers occur for no consideration,²⁹ so even if there was no supply by way of sale requirement, the available deduction would be zero.

Situated in New Zealand

88. For a person to claim a secondhand goods input tax deduction on the supply of goods the goods must be situated (located) in New Zealand at the time of supply.
89. Where the goods are situated is a question of fact.
90. The "time of supply" for a supply of goods is defined in s 9. It is generally the earlier of the time an invoice is issued or the time any payment is received by the supplier. See [106] for what constitutes a "payment".
91. Where goods are situated outside New Zealand at the time of supply and then imported into New Zealand, the importer may be charged GST by the New Zealand Customs Service and be allowed a deduction under s 3A(1)(b), but the secondhand goods input tax deduction is not involved.
92. The test of whether goods are situated in New Zealand is different from the test of whether a supply is made in New Zealand. A supply being made in New Zealand is a requirement for the charging of GST under s 8 (which is of limited relevance to the claiming of secondhand goods input tax deductions). Section 8 sets out a number of legal tests for determining whether a supply is made in New Zealand. Under s 8, whether a supply is made in New Zealand depends on, among other factors, the residence of the supplier and the location of the goods at the time of supply.

The supply must not have been a taxable supply

93. For a purchaser to claim a secondhand goods input tax deduction, the supply to the purchaser must not be a taxable supply.³⁰
94. A supply is not a taxable supply if it is:³¹
 - not made by a registered person;
 - an exempt supply;
 - not made in the course or furtherance of a taxable activity; or
 - not made in New Zealand.

Supply is not made by a registered person

95. For a purchaser to claim a secondhand goods input tax deduction, the supply to the purchaser must not be a taxable supply. A supply is not a taxable supply if it is not made by a "registered person".³²

29 The supplies are not treated as being made at market value under s 10(3). The supplies are not associated supplies. A deceased person and their estate, and the estate and a beneficiary, are not associated persons. The mere fact a person has died, and an executor or administrator has been appointed to manage their estate does not give rise to a trust relationship of settlor and trustee, or trustee and beneficiary. For a transfer made subject to a testamentary trust, see s 10(3A).

30 Section 3A(2)(a).

31 Definition of "taxable supply" in s 2, and s 8.

32 Section 8(1).

96. The term registered person includes a person who is liable to be registered, even if they have not applied to be registered or have not been registered by the Commissioner.³³
97. This is illustrated in Example | Tauira 12.

Example | Tauira 12 – Supplier liable to be a registered person

Satoji likes to work on cars. He regularly buys cars, completes repairs and then sells them for a profit. In the current month, and in the preceding 11 months, Satoji made supplies of cars totalling \$80,000. Satoji intends to continue this activity at this level in the next 12 months.

Satoji sells one of the cars to a GST-registered used-car dealer for \$11,500 including GST (if any). At the end of the month when preparing the GST return, the manager of the used-car dealer considers whether they can claim an input tax deduction on the purchase of the car.

Satoji has not applied to be registered for GST, but he is potentially liable to be registered. A person who is liable to be registered is a registered person, even if they have not applied to be registered or have not been registered by the Commissioner. If Satoji is a registered person, the used car dealer is unable to claim a secondhand goods input tax deduction.

The manager knows Satoji has been selling a few cars lately, so suggests Satoji check whether he is liable to register.

Satoji realises he became liable to register for GST four months ago and applies to the Commissioner for registration. The Commissioner registers Satoji for GST from the date he was first liable to be registered.

Satoji then issues the used car dealer taxable supply information for the supply of the car.

Satoji is liable to return GST of \$1,500 ($\$11,500 \times 3/23$) on the supply of the car and the used car dealer can claim a standard input tax deduction for this GST.

The supply is an exempt supply

98. For a purchaser to claim a secondhand goods input tax deduction, the supply to the purchaser must not be a taxable supply. A supply is not a taxable supply if it is an exempt supply.

Supply by non-profit body of donated goods

99. One example of an exempt supply is supply by a non-profit body of donated goods and services (this kind of supply is exempt even if the non-profit body is registered for GST).³⁴
100. If a registered person purchases goods from a non-profit body that were donated to the non-profit body, the purchaser may be able to claim a secondhand goods input tax deduction. This is illustrated in Example | Tauira 13.

Example | Tauira 13 – Supply by a non-profit body of donated goods

Paws and Claws Trust is a non-profit body that catches and re-homes feral kittens. The trust is registered for GST.

The trust receives a donation of a used car. The car is not suitable for the trust's activities, so the trust lists the car for sale. In its advertisement, the trust notes, "GST Registered person? This is a donated good – a secondhand input tax deduction may be available".

Cleo, who is registered for GST, is looking to buy a used car for use in her accounting business. She finds two cars she could buy: the trust's car and a car being sold by a used-car dealer. She slightly prefers the trust's car. The trust has listed its car for \$15,000 (with no GST because the supply of the car is not taxable) and the used car dealer has listed its car for \$15,000 including GST.

Preferring the trust's car and knowing she can claim a secondhand goods input tax deduction, Cleo chooses to purchase the trust's car.

³³ Definition of "registered person" in s 2.

³⁴ Section 14(1)(b).

Property used for exempt supplies of accommodation

101. The sale of a property by a GST registered supplier can be an exempt supply if the property was used by the supplier for exempt supplies of accommodation for at least five years immediately before the sale.³⁵ Because the supply is exempt and, therefore, not taxable, a registered person who purchases such a property for making taxable supplies (for example, if the property was used as a business premises rather than being used for exempt supplies of accommodation) could potentially claim a secondhand goods input tax deduction. This is illustrated in Example | Tauira 14.

Example | Tauira 14 – Property used for exempt supplies of accommodation for at least five years

Agnes decides to start a cattery business. She purchases a residential property, which she will convert into a cattery. Agnes has registered for GST and has purchased the property for making taxable supplies in the course of her planned taxable activity.

The supplier of the property is registered for GST, but the property was rented as a residential dwelling for the last seven years. Because of this prior use, the supply is not taxable, so the vendor does not include GST in the purchase price.

Agnes' conveyancing lawyer checked the GST treatment with the vendor's lawyer, so Agnes is aware of the previous use and is aware it means she can claim a secondhand goods input tax deduction for the purchase of the property.

Supply not made in the course or furtherance of a taxable activity

102. For a purchaser to claim a secondhand goods input tax deduction, the supply to the purchaser must not be a taxable supply. A supply is not a taxable supply if it is not made in the course or furtherance of the taxable activity the supplier carries on.³⁶ This is illustrated in Example | Tauira 15.

Example | Tauira 15 – Supply not made in the course or furtherance of a taxable activity

Ethan is a contractor who supplies services to a government department. Because of the amount he invoices the department each year, he is registered for GST.

Ethan has a car that he uses privately. He does not use it for making his supplies.

Ethan sells his car to a used car dealer for \$11,500. The supply of the car is not made in the course or furtherance of Ethan's taxable activity because the car was not part of the activity. Therefore, despite Ethan being registered for GST, the supply of the car is not a taxable supply, and Ethan does not need to charge GST on the supply.

The used car dealer can claim a secondhand goods input tax deduction of \$1,500 ($\$11,500 \times 3/23 = \$1,500$) on the purchase of the car.

Supply not made in New Zealand

103. For a purchaser to claim a secondhand goods input tax deduction, the supply to the purchaser must not be a taxable supply. A supply is not a taxable supply if it is not made in New Zealand.³⁷

104. Whether a supply of goods is made, or treated as being made, in New Zealand depends on various factors:³⁸

- If the supplier is resident in New Zealand, then the supply is made in New Zealand.
- If the supplier is not resident in New Zealand and the goods:
 - are not in New Zealand at the time of supply, then the supply is not made in New Zealand and, therefore, is not a taxable supply, but in that case, a secondhand goods input tax deduction would not be available because of the separate requirement for the secondhand goods input tax deduction that goods are situated in New Zealand (see [88]);³⁹

³⁵ Section 14(1)(d).

³⁶ Section 8.

³⁷ Section 8.

³⁸ Section 8(2) to (4).

³⁹ Section 3A(2).

- are in New Zealand at the time of supply, and if the supply is made to a registered person for the purposes of carrying on the registered person's taxable activity (which is required anyway for the secondhand goods input tax deduction), then the goods and services are treated as being supplied outside New Zealand, unless the supplier chooses to treat the supply as made in New Zealand.

105. This means it is possible for a supply by a non-resident of goods situated in New Zealand to be treated as not supplied in New Zealand and, therefore, for the supply to not be a taxable supply. In this situation, the purchaser of the goods could potentially claim a secondhand goods input tax deduction. This is illustrated in Example | Taura 16.

Example | Taura 16 – Supply not made in New Zealand

Mei is non-resident and has equipment in New Zealand that she sells to Melanie, a registered person who acquires the equipment for the purposes of carrying on a taxable activity.

Mei does not choose to treat the supply as made in New Zealand. Therefore, the supply of the equipment to Melanie is treated as being made outside New Zealand and is not a taxable supply.

Because the supply is not a taxable supply, Melanie is able to claim a secondhand goods input tax deduction for the equipment.

Payment

106. Section 20(3) allows a deduction "to the extent that" a payment in respect of a supply has been made during the taxable period. This is illustrated in Example | Taura 17.
107. If part of the payment has been made during a taxable period, a deduction is allowed in the period for that part.
108. The meaning of payment is discussed in **IS 25/23: GST – meaning of payment**.⁴⁰ IS 25/23 discusses the meaning of payment for the purposes of the Act generally. The meaning of payment is also relevant in other contexts, including for rules that apply to persons who account for GST on a payments or hybrid basis, and for the time of supply rules.
109. Refer to IS 25/23 for a more detailed discussion, but the meaning of payment can be summarised as follows:
- A payment can be made with money or by transferring property or providing services (for example, a company could make a payment by issuing shares in itself to a supplier).
 - Payment can be made using a promissory note or a bill of exchange. A mere acknowledgement of debt is not sufficient.
 - Payment will not be made if the purchase price for the supply of goods or services is simply deferred or left owing under the supply agreement.
 - Payment could be made by the purchaser borrowing an amount under a separate agreement with the supplier (or another person) and using the amount borrowed to satisfy the payment obligation under the supply agreement. By doing this, payment will be made for GST purposes, even though the purchaser will still owe the supplier an amount under the separate loan agreement.
 - Payment for a supply could be made by set-off against an existing debt owed by the supplier to the recipient. For example, if the supplier owed the recipient an amount under an existing debt, the amount payable by the recipient for the supply could be offset against the amount owed by the supplier to the recipient.
 - Accounting entries can provide at least some evidence that a payment has occurred. However, accounting entries may not always be sufficient. The absence of accounting entries does not mean a payment has not been made. However, depending on other evidence available, the timing of the accounting entries could influence the determination of when the payment was made.
 - The payment of a deposit under an agreement constitutes a payment.
 - Where the recipient of a supply makes a payment to a stakeholder, for GST purposes, the recipient has not made a payment. Payment will not occur until the stakeholder's obligations are at an end and the amount is held for the supplier's benefit.

⁴⁰ IS 25/23: GST – meaning of payment.

Example | Taura 17 - Input tax only allowed to the extent payment is made

Frank is registered for GST on a six-monthly basis (March and September).

Frank acquires land from an unregistered vendor for \$1 million, with a deferred settlement. Frank plans to use the land in his taxable activity. Frank pays a \$100,000 deposit in March 2026. Settlement occurs in September 2026, where the balance of the purchase price is paid.

Assuming the other requirements for a secondhand goods input tax deduction are satisfied, Frank can claim a secondhand goods input tax deduction as follows:

- In the GST period ended 31 March 2026, input tax of \$13,043 on the \$100,000 deposit ($\$100,000 \times 3/23$).
- In the GST period ended 30 September 2026, \$117,391 on the balance of \$900,000 ($\$900,000 \times 3/23$).

Frank is not entitled to claim input tax on the full \$1 million purchase price in the March 2026 GST return. At this point in time, Frank had only made payment of the deposit. A secondhand goods input tax deduction is only allowed to the extent that payment has been made.

Records required

110. For a person to claim a secondhand goods input tax deduction on the purchase of a secondhand good, they must have a record of the supply showing:⁴¹

- the name and address of the supplier;
- the date on which the secondhand goods were supplied;
- a description of the secondhand goods;
- the quantity or volume of the secondhand goods; and
- the consideration for the supply.

111. This requirement does not apply to a supply if the consideration for the supply is equal to or less than \$200.

Exception – goods acquired before 1 October 1986

112. A registered person is not allowed a secondhand goods input tax deduction for the purchase of goods if the purchase is of goods that were acquired before 1 October 1986 by the registered person or, more likely, by a person who, when acquiring the goods, was associated with the registered person.⁴² This is illustrated in Example | Taura 18.

113. However, this does not apply if the goods have been owned, on or after 1 October 1986, by a person who, at the time, was not the registered person and was not associated with the registered person. This is illustrated in Example | Taura 19.

Example | Taura 18 – Associated supplier who purchased the land before 1 October 1986

Jim is Barry's father. Jim purchased a block of land in 1982. Jim, who is not registered for GST, recently sold the land to Barry.

Barry, who had been born when Jim bought the land in 1982, is registered for GST and has purchased the land to make taxable supplies.

Barry is not allowed a secondhand goods input tax deduction for the land. This is because Jim purchased the land before 1 October 1986, and Barry and Jim were associated persons when Jim purchased the land.⁴³

Variation

If Barry had not been born in 1982 when Jim bought the land, the exception in s 3A(2)(ab) would not apply. This is because when Jim purchased the land, he and Barry would not have been associated. This would mean Barry could potentially claim a deduction (if other requirements are satisfied).

⁴¹ Sections 19H and 20(2)(c). See also New Legislation *Tax Information Bulletin* Vol 34, No 5 (June 2022): 3 at 159.

⁴² Section 3A(2)(ab).

⁴³ Section 2A(1)(c)(i).

Example | Taura 19 – Intervening non-associated person owner

The trustees of the Wensleydale Trust purchased a block of land in 1984.

Patricia is a beneficiary of the Wensleydale Trust and has been since before the land was purchased in 1984.

In 1987, the trustees of the trust sold the land to Henry, another beneficiary of the trust and Patricia's cousin. Recently, Patricia purchased the block of land from Henry, who is not a registered person. Patricia and Henry are not associated persons (association between relatives extends only to the second degree of relationship, cousins are separated by four degrees). Patricia is registered for GST and has purchased the land to make taxable supplies.

Patricia is potentially able to claim a secondhand goods input tax deduction. Despite being associated with the trustees of the trust when the land was purchased in 1984 (before 1 October 1986), someone else, who Patricia was not associated with, has owned the land since 1 October 1986.

Exception – supply of previously-leased imported goods

114. A purchaser is not allowed a secondhand goods input tax deduction if the exception described below applies. The exception applies where:⁴⁴

- a non-resident lessor supplies goods by way of lease to a New Zealand resident lessee who is registered for GST;⁴⁵
- the lessee imports the goods into New Zealand; and
- the lessor⁴⁶ later sells the goods to a New Zealand resident purchaser.

115. This is illustrated in Diagram | Hoahoa 3.

116. In this situation, the exception prevents the New Zealand resident purchaser from claiming a secondhand goods input tax deduction. This is to prevent two input tax deductions being claimed when only one amount of tax is charged. This can be explained as follows:

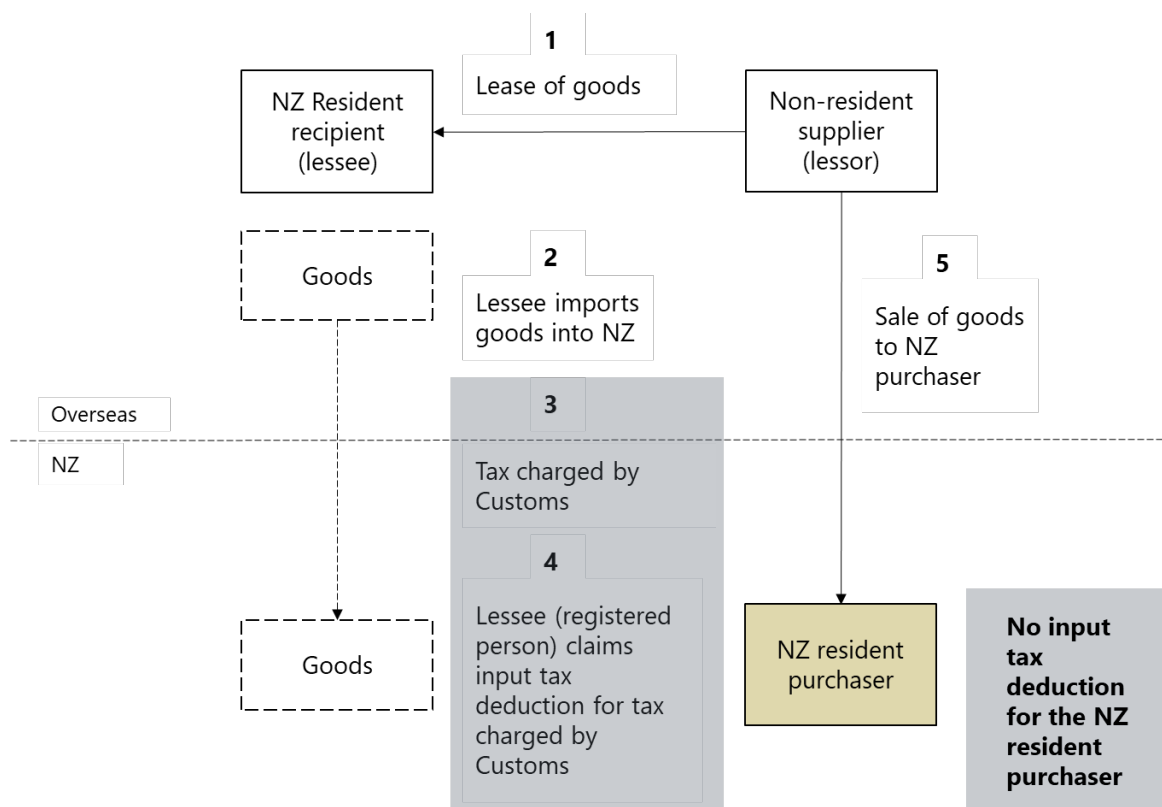
- Tax is charged by the New Zealand Customs Service when the goods are imported.
- Tax might not be charged on the supply by the non-resident lessor to the New Zealand resident purchaser. This is because the supply might be treated as not being made in New Zealand.⁴⁷
- The lessee, who imported the goods, may have claimed an input tax deduction for the customs GST paid.
- In the absence of the exception, the New Zealand resident purchaser could potentially claim an additional input tax deduction – in the form of a secondhand goods input tax deduction (given the supply by the lessor to the New Zealand resident purchaser is not a taxable supply and the goods are situated in New Zealand).

44 Section 3A(2)(b). The wording of s 3A(2)(b) does not refer to a supply by way of lease. However, this is the intended application of the imported goods exception, which was discussed in New Legislation *Tax Information Bulletin* Vol 24, No 10 (December 2012): 18 at 39. The application to a supply by way of lease followed by a supply by way of sale is also consistent with the split between subparas (i) and (ii) of s 3A(2)(b).

45 The exception also applies if the New Zealand recipient is not registered when the goods are imported (so does not claim an input tax deduction for the customs GST), but later registers for GST and claims an input tax deduction under s 21B for a change in use of the goods.

46 The imported goods exception also applies if the non-resident lessor has sold the goods to another non-resident who sells the goods to the New Zealand resident purchaser.

47 Under s 8(4). The requirements of the subsection could be satisfied because the lessor is non-resident, the goods are supplied to the New Zealand resident purchaser for the purposes of carrying on their taxable activity, and the lessor may not have chosen to treat the supply as made in New Zealand.

Diagram | Hoahoa 3 – Supply of previously-leased imported goods

Exception – zero-rated financial services

117. A person is not allowed a secondhand goods input tax deduction if the goods are acquired for making taxable supplies of financial services that are zero-rated under s 11A(1)(q) or s 11A(1)(r). This exception does not apply if, before the acquisition, the goods have never been owned or used by the purchaser or an associated person.⁴⁸

118. The purpose of this exception is to prevent large one-off input tax credits from the transfer of existing assets (for example, land) from an entity that is exempt to an associated entity that will use the assets to make zero-rated taxable supplies.⁴⁹

Restrictions on the amount of deduction allowed

119. The secondhand goods input tax deduction a person can claim on a supply they receive is based on the amount of “input tax” for the supply. In the case of secondhand goods input tax deductions, input tax is an imputed amount.

120. The amount⁵⁰ of input tax depends on whether the:

- person and supplier are associated persons;⁵¹
- supplier is deemed to have made a supply of the goods under s 5(3) (s 5(3) deems a person to make a supply of goods forming part of their taxable activity if they cease to be a registered person); and
- supply is the only matter to which consideration provided relates.

121. Situations involving these factors are discussed below.

⁴⁸ Section 3A(2)(c). The wording of s 3A(2)(c) is not entirely clear. However, the context suggests that subparas (i) and (ii) of s 3A(2)(c) concern the subsequent taxable supplies that a person makes, not the supply to the person for which the secondhand goods input tax deduction is sought. This is supported by the context provided by the secondhand goods input tax deduction requirement that the supply is not a taxable supply – if a supply is not a taxable supply, there would be no occasion for the supply to be zero-rated. See also A McKenzie, *GST: A Practical Guide* (e-book, 10th ed, CCH, 2017) at 312.

⁴⁹ See Taxation (Annual Rates, GST, Trans-Tasman Imputation and Miscellaneous Provisions) Bill: Commentary to the Bill (Policy and Advice Division, Inland Revenue, June 2003) at 4.

See also Taxation (Annual Rates, GST, Trans-Tasman Imputation and Miscellaneous Provisions) Bill: Officials’ report to the Finance and Expenditure Committee on submissions on the Bill (Policy and Advice Division, Inland Revenue, and The Treasury, October 2003) at 20.

⁵⁰ This is often referred to as the quantum of input tax allowed.

⁵¹ The meaning of “associated persons” is discussed at [151].

Supplier and recipient are not associated

122. If the supplier and the recipient are not associated, the calculation of input tax for a supply depends on whether the supply is the only matter to which the consideration provided by the recipient relates.
123. Sometimes a single amount of consideration is provided for the supply of a good and for something else without specifying how much is paid for the supply of the good and how much is paid for the other thing. In these situations, the input tax for the supply of the good is the lesser of the tax fraction of the:⁵²
- purchase price for the good (the single amount of consideration must be apportioned between the good and the other thing); and
 - open market value of the good.
124. This is illustrated in Example | Tauria 20.
125. If the consideration is provided for the good only, the input tax is the tax fraction of the “consideration in money” for the good.
126. “Consideration in money” is defined in s 2:
- consideration in money** includes consideration expressed as an amount of money
127. Consideration in money is an inclusive definition, so the ordinary meaning of the words (having regard to the definition of consideration) applies, and this ordinary meaning is extended by the definition.
128. Because the ordinary meaning of the words applies, an amount of consideration is “consideration in money” if provided in the form of money. “Money” is defined in s 2. This is also an inclusive definition. Money, among other things, includes cash, a credit in a bank account and cheques (when they were still used).
129. However, the extended meaning provided by the definition of consideration in money means that consideration in money can also be non-monetary, provided the consideration is “expressed as an amount of money”. For example, a person is selling a section of land and part of the consideration provided by the purchaser is an agreement to provide earthmoving services to the value of \$100,000. These services are non-monetary consideration expressed as an amount of money.
130. The Act does not explain what it means for an amount to be “expressed as an amount of money”. Based on the ordinary meaning, there is no requirement for a statement in writing expressing an amount as money. However, if there is no statement in writing, it may be harder to establish that an amount was expressed as an amount of money.
131. In the Commissioner view, the amount expressed in money should reflect the open market value of the non-monetary consideration (consistent with s 10(2)(b)(i)). In the secondhand goods context, which involves a non-taxable supply and often a non-registered supplier, a supplier may be indifferent to the amount expressed in money for the non-monetary consideration they receive because they will have no GST liability. With non-registered suppliers there also may not be standard pricing associated with the goods supplied, from which a value might be inferred. Therefore, without further evidence, the Commissioner may not always accept that the amount expressed in money reflects the open market value of the non-monetary consideration.
132. The Commissioner will accept reasonable efforts, corresponding with the size of the transaction, to determine open market value. For example, where the non-monetary consideration is an agreement to provide earthmoving services to the value of \$100,000, invoices showing amounts charged to previous customers for similar services (on an arm’s length basis) could be sufficient to establish the open market value.

⁵² Section 3A(3)(d). The meaning of “tax fraction” is discussed at [155]. It is generally 3/23, reflecting the current GST tax rate of 15%.

Example | Taura 20 – Consideration provided for a supply of a good and for something else

Keith, who is not registered for GST, sells a secondhand bandsaw to James and agrees to provide James four hours of valuable woodworking instruction. James is registered for GST and acquires the bandsaw and the training to make taxable supplies in his joinery business.

Keith and James are old friends, so Keith gives James a discount, charging him \$1,000 for both the saw and the training (with no breakdown of how much is paid for the saw and for the training). The open market value of the saw and training would normally be \$900 and \$225, respectively.

In this case, a single amount of consideration has been provided for two things. Therefore, the secondhand goods input tax deduction that James can claim for the saw is limited to the lesser of the tax fraction of the purchase price of the saw (this requires apportionment) and the tax fraction of the open market value of the saw.

In this case, for the apportionment of the purchase price, James treats \$800 of the amount paid to Keith as the purchase price of the saw and \$200 as a fee for the training. This appears reasonable in the circumstances as it is proportionate to the undiscounted value of the supplies.

Although the open market value of the saw would normally be \$900, here a discount has been given on an arm's length basis (Keith and James, although friends, are not associated persons). A discounted price can still be a market price. So, it is appropriate to allocate the amount paid between the saw and the training on a reasonable basis to identify the open market value for this transaction. On this basis, the \$800 amount determined by James could also be seen as the open market value of the saw.

James can claim a secondhand goods input tax deduction for the purchase of the bandsaw. However, the input tax for this supply is limited to \$104.35, the tax fraction of the \$800 purchase price allocated to the saw ($\$800 \times 3/23 = \104.35).

Supplier and recipient are associated, no deemed supply under s 5(3)

133. If the recipient and the supplier are associated persons and the supplier is not deemed to have made a supply of the goods under s 5(3), the amount of input tax is the lowest of:⁵³

- either:
 - if the supplier also received the goods from an associated person, the amount given by s 3A(3BB);⁵⁴ otherwise
 - the tax fraction⁵⁵ of the original purchase price⁵⁶ of the goods when they were received by the supplier (that is, the purchase price for the supplier's acquisition of the goods);⁵⁷
- the tax fraction of the purchase price,⁵⁸ and
- the tax fraction of the open market value of the supply.

134. This is illustrated in Diagram | Hoahoa 4 and Example | Taura 21.

135. For the avoidance of doubt, if the original purchase price of the goods when they were received by the supplier was zero, then the input tax deduction will be zero. For example, if the supplier received the goods as a distribution from a trust, the input tax deduction for the associated person who acquires the goods from the supplier would be zero.

53 Section 3A(3)(a).

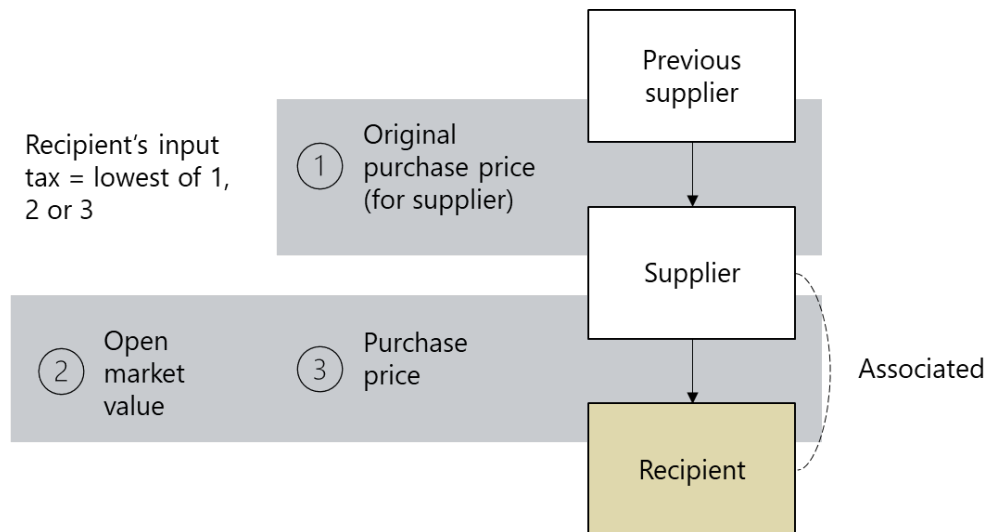
54 Section 3A(3BB) is discussed at [136].

55 Depending on when the goods were received by the supplier, the tax fraction could be 3/23, 1/9 or 1/11. See from [111].

56 The meaning of "original purchase price" is discussed at [145].

57 Section 3A(3)(a)(i). This subpara has been amended several times. Before 30 March 2022, it referred to "the tax included in the original cost of the goods to the supplier", which is quite different from the current wording, which can include an imputed amount. Under the current wording, if the supplier had acquired the goods from an unregistered person, there could be an imputed amount given by the tax fraction of the original purchase price paid by the supplier. The tax fraction given by s 3A(3BB) is discussed at [136].

58 The meaning of "purchase price" is discussed from [139].

Diagram | Hoahoa 4 – Input tax where supplier and recipient are associated, no s 5(3) supply**Example | Tauira 21 – Land sold to associated company**

In 2025, Henry sold a block of land to a company for \$1.5 million (this is also the open market value of the land). Henry had a 30% voting interest in the company when he sold the land.

Henry had bought the land from a non-registered third party for \$1.3 million two years earlier with the intention of building a house and living on the land. However, for the last two years, Henry has just been leasing the land to a neighbour for grazing. Henry has never been registered for GST and was not liable to be registered when he sold the land.

At the time of the supply, Henry and the company were associated persons because Henry had voting interests of 25% or more in the company.

The amount the company can claim is the lowest of the tax fraction of the:

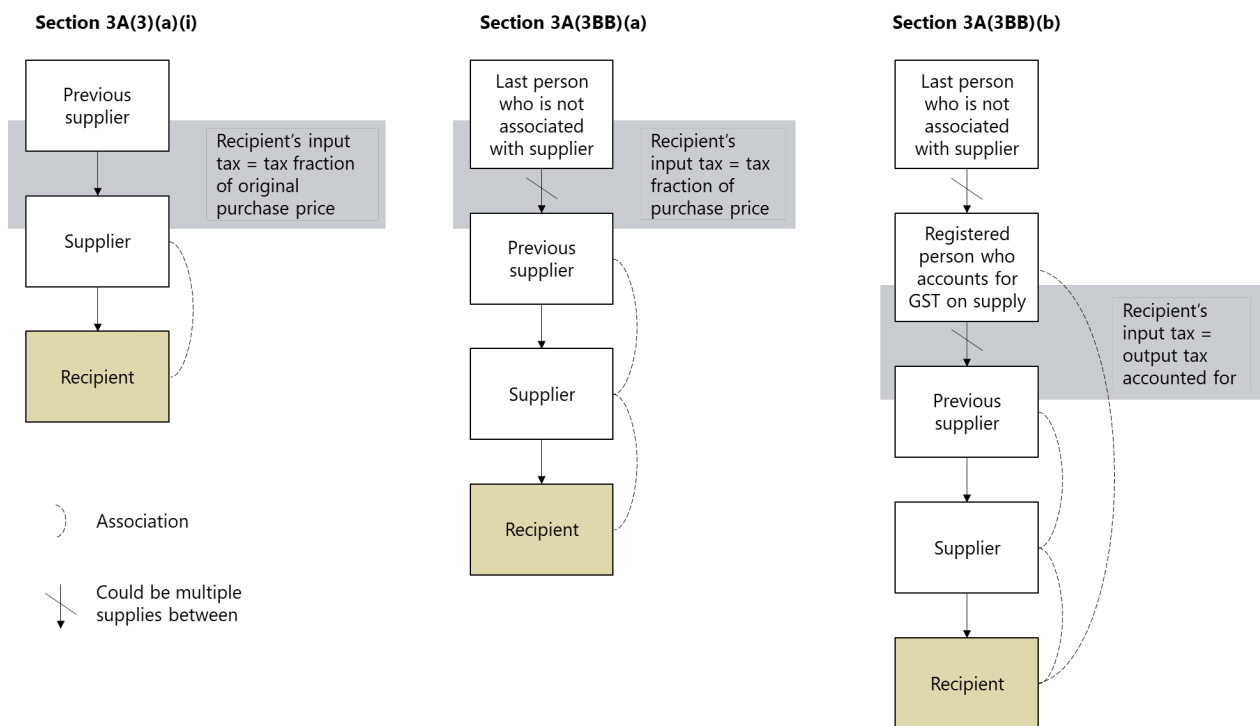
- \$1.3 million original purchase price Henry paid for the land;
- \$1.5 million purchase price the company pays to Henry; and
- \$1.5 million open market value of the land.

Therefore, the amount the company can claim is 3/23 of \$1.3 million, which is \$169,565.22.

The company can claim a deduction for an imputed amount despite GST not being charged on the supply from the third party to Henry.

Where the supplier also received the goods from an associated person – s 3A(3BB)

136. Section 3A(3BB) applies if the supplier also received the goods from an associated person. In this case, the amount of input tax is generally the tax fraction of the purchase price of the goods when they were last supplied by a person who is not associated with the supplier. A different input tax amount applies if, after the last supply by a person who is not associated with the supplier and before the associated supply being considered, the goods were supplied by a registered person associated with the supplier and the registered person accounted for output tax on the supply. In that case, the amount of the input tax is an amount equal to the amount of output tax accounted for. This is illustrated in Diagram | Hoahoa 5 and Example | Tauira 22.

Diagram | Hoahoa 5 – Where the supplier also obtained the goods from an associated person – s 3A(3BB)**Example | Tauira 22 – Multiple associated supplies**

In 2008, Kaea bought an apartment for \$300,000 from her friend Travis.

Kaea has two daughters, Kara and Koa.

In 2010, Kaea settled the apartment on a family trust. Kaea was trustee and Kara and Koa were beneficiaries of the trust.

In 2015, the family trust sold the apartment to Kara for \$350,000.

In 2025, Kara sold the apartment to her younger sister Koa for \$500,000.

None of Travis, Kaea, the family trust or Kara was registered for GST. However, Koa is registered, and she intends to use the apartment to make taxable supplies in her physiotherapy practice.

Koa can claim a secondhand goods input tax deduction for the purchase of the apartment, but the amount is limited to \$33,333.33, the tax fraction of the purchase price Kaea paid for the apartment ($\$300,000 \times 1/9 = \$33,333.33$).⁵⁹

Section 3A(3BB)(a) applies because Koa acquired the apartment from an associated person (her sister Kara) and Kara also acquired the apartment from an associated person (the trustee of the family trust). Koa is associated with the family trust and her mother Kaea, so Travis was the last person who was not associated with Kara. This means the input tax for the supply made by Kara to Koa is calculated based on the tax fraction of the purchase price Kaea paid to Travis.

Variation

This variation uses the same facts as above except Kaea registered the family trust for GST, as trustee carried on a taxable activity from the apartment and, when the apartment was sold, accounted for \$45,652.17 of GST on the supply of the apartment to Kara.

In this case, Koa's secondhand goods input tax deduction is limited under s 3A(3BB)(b) to the \$45,652.17 of output tax accounted for by the family trust when it supplied the apartment to Kara.

⁵⁹ The tax rate was 12.5% when Kaea purchased the apartment, so the tax fraction is 1/9 rather than 3/23.

Supply involving land and an arrangement with more than two associated parties and more than one supply

137. An exception to s 3A(3)(a) applies if a supply wholly or partly consists of land and is part of an arrangement involving more than two associated parties and more than one supply.⁶⁰ In this case, the input tax for the recipient is limited by the amount accounted for as output tax for all supplies that are part of the arrangement.
138. For a supply of land to be part of an arrangement involving multiple supplies, there would need to be some sort of plan or linkage between the different supplies or steps in the arrangement.⁶¹

Meaning of “consideration” and “purchase price”

139. The definition of input tax in s 3A refers to both the “consideration” for a supply (in s 3A(3)(d) and (e)) and the “purchase price” of the goods (in s 3A(3)(a)(ii), (b)(ii), (c)(ii) and (d)(i)). The definition also refers to “consideration in money” (in s 3A(3)(e)).
140. “Consideration” and “consideration in money” are defined in s 2:
- consideration**, in relation to the supply of goods and services to any person, includes any payment made or any act or forbearance, whether or not voluntary, in respect of, in response to, or for the inducement of, the supply of any goods and services, whether by that person or by any other person; but does not include any payment made by any person as an unconditional gift to any non-profit body
- consideration in money** includes consideration expressed as an amount of money
141. However, “purchase price” is not defined.
142. It is not entirely clear what the difference is between “consideration” and “purchase price” in the context of s 3A(3). The context provided by s 3A(3)(d) might suggest (generally – for all of s 3A(3)) that the difference arises where the supply is not the only matter to which the consideration relates; in which case purchase price might refer only to the portion of the consideration that relates to the supply.⁶²
143. Further, it appears that purchase price and consideration in s 3A(3) can include monetary and non-monetary payments made for the supply of the goods.
144. In s 3A(3), the phrase consideration in money is used only in s 3A(3)(e), the catch-all provision that states that in all other cases, the amount of input tax is the tax fraction of the consideration in money for the supply. However, even in that case, consideration can be non-monetary, provided the consideration is “expressed as an amount of money”. For example, the consideration could be expressed as being services to the value of \$10,000.

Meaning of “original purchase price”

145. The Commissioner considers that the “original purchase price of the goods when they were received by the supplier” can include the purchase price of multiple supplies that have been used to produce the current good. For example, the original purchase price of a property could include the purchase price of the land and the cost of erecting a building on the property.
146. If the good received by the registered person consist of only part of a good received by the supplier when the supplier acquired the good, an apportionment is required to calculate the original purchase price.
147. This is illustrated in Example | Tauria 23.

⁶⁰ Section 3A(3B).

⁶¹ “Arrangement” is not defined for the purposes of s 3A(3B). However, it is considered a court is likely to interpret the word arrangement in this context in a similar way as it is used in s 76, the general anti-avoidance provision in the Act. The meaning of “arrangement” is discussed in IS 23/01: Tax avoidance and the interpretation of the general anti-avoidance provisions sections BG 1 and GA 1 of the Income Tax Act 2007 *Tax Information Bulletin* Vol 35, No 2 (March 2023): 8.

⁶² This appears to be consistent with the view taken in A McKenzie, *GST: A practical guide* (e-book, 10th ed, CCH, 2017) at 302.

Example | Tauira 23 – Original purchase price where there are renovations and extension to a property

Sean, who is not registered for GST, purchases a run-down property for \$1.1 million. Sean subdivides the property into two sections. After the subdivision, the section containing the property is valued at \$690,000 and the other section is valued at \$450,000.

Sean then spends another \$460,000 on renovations and an extension to the property.

Ten years later, Sean and his partner incorporate a company, which is starting an early learning centre. Sean, still not a registered person, sells the section containing the property to the company for \$1.38 million (which is the open market value). The company intends to use the property as the premises for the early learning centre.

The company can claim a secondhand goods input tax deduction, but this will be limited to the tax fraction of the original purchase price of the property.

The original purchase price of the property includes a portion of the \$1.1 million amount Sean paid for the land before it was subdivided and the \$460,000 spent on renovations and the extension to the property.

The portion of the \$1.1 million purchase price can be calculated based on the relative values of the two sections after subdivision: $\$690,000 / (\$690,000 + \$450,000) \times \$1.1 \text{ million} = \$665,789$.

This combined with the \$460,000 spent on renovations and the extension to the property gives an original purchase price of \$1,125,789. The tax fraction of this is \$146,842. This is the secondhand goods input tax deduction the company can claim.

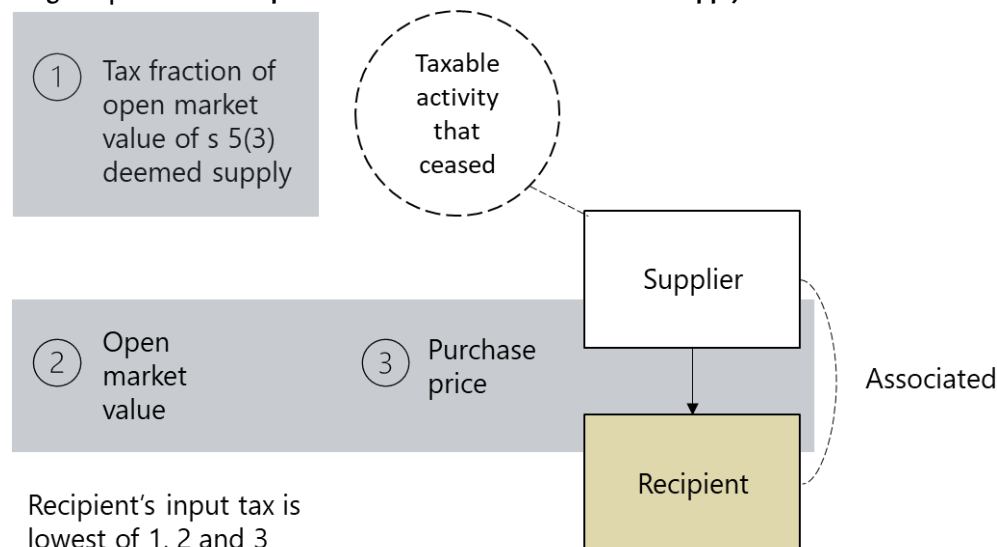
Supplier and recipient are associated, deemed supply under s 5(3)

148. The calculation of input tax is different if the associated supplier was previously a registered person and was treated under s 5(3) as making an supply of the goods when they ceased to be registered. Under s 5(3), where a person ceases to be a registered person, any goods then forming part of their taxable activity are deemed to be supplied by that person in the course of that taxable activity (despite in fact retaining the goods).

149. If the supplier and the recipient are associated persons and the supplier is deemed to have made a supply of the goods under s 5(3), then the input tax is the lowest of the tax fraction of the:⁶³

- open market value of the deemed supply under s 5(3) (or the tax fraction of the valuation under s 10(8) if the supply was valued under that subsection);
- purchase price; and
- open market value of the supply.

150. This is illustrated in Diagram | Hoahoa 6 and Example | Tauira 23.

Diagram | Hoahoa 6 – Input tax restricted because of deemed supply on cessation of taxable activity

⁶³ Section 3A(3)(c).

Example | Taura 24 – Selling business assets after cessation to associated company

Albert operated a café business for several years but last year had to close the café. When the café closed, Albert ceased his GST registration. As a result, under s 5(3), Albert was treated as making a deemed supply (not an actual supply) of the café assets that he retained. This included the retail property from which he ran the café. The open market value of the property at the time of the deemed supply was \$300,000.

Albert has just sold the property for \$350,000 to Always Coffee Ltd, which is opening a new café. The sale price of \$350,000 reflects the open market value of the property. Albert has voting interests of 30% in Always Coffee Ltd, so Albert is associated with the company at the time of supply.⁶⁴

Always Coffee Ltd can claim a secondhand goods input tax deduction. However, because Albert is associated with the company, the company's secondhand goods input tax deduction is restricted to \$39,130.43 ($\$300,000 \times 3/23$), being the tax fraction of the \$300,000 open market value of the deemed supply that occurred last year when Albert's taxable activity ceased under s 5(3).

Associated persons

151. In some cases, the calculation of input tax depends on whether two persons (usually the supplier and the recipient) are associated. For GST purposes, whether two persons are associated is determined by the definition of "associated persons" in s 2A.
152. Determining whether two persons are associated is complex, so we don't discuss the definition of "associated persons" in detail here. Read the definition in s 2A and obtain advice if necessary. Some guidance is in **A guide to associated persons definitions for income tax purposes – IR620**. IR620 specifically considers the meaning of associated persons for income tax purposes but given the similarity of the tests in the Income Tax Act 2007 and the GST Act, it may provide some assistance.
153. In very simple terms and without being exhaustive, associated persons include:
 - companies controlled to the extent of 50% or more by the same group of persons;
 - a company and a person with a 25% or greater interest in the company;
 - a partnership and a partner of the partnership;
 - a joint venture and a member of the venture;
 - relatives by blood (to the second degree), marriage, civil union, de facto relationship or adoption;
 - trustees of a trust and persons who have benefited or are eligible to benefit under the trust;
 - trustees and the settlor of a trust, except where the trustee is a charitable or non-profit body;
 - trustees of two trusts that have a common settlor; and
 - two persons if they are each associated with a common third person (tripartite test).
154. The definition also features an aggregation rule for company ownership interests⁶⁵ that can apply where two persons are associated. Each person can be treated as holding the company ownership interests that the other holds as well as their own, which may result in a threshold being reached for company association.

Tax fraction

155. In the context of secondhand goods input tax deductions, where no GST is charged by the supplier, input tax is an imputed amount calculated based on the tax fraction of the relevant amount (for example, the tax fraction of the purchase price).
156. The tax fraction is usually 3/23, which reflects the current GST tax rate of 15%. However, in some cases a different tax fraction applies because (as discussed below) input tax is sometimes calculated by reference to a purchase price or valuation that was paid or made in the past when a different GST rate applied.⁶⁶

⁶⁴ Section 2A(1)(b)(i).

⁶⁵ Section 2A(4).

⁶⁶ Section 3A(5) states that for the purpose of s 3A(3), tax fraction means the tax fraction that applies at the time of supply.

157. The history of the changes in the GST tax rate and the corresponding tax fractions are summarised in the Table | Tūtohi 1.

Table | Tūtohi 1 – History of tax rates and tax fractions

When the supplier received the goods	Tax rate	Tax fraction
On or after 1 October 2010	15.0%	3/23
Between 1 July 1989 to 30 September 2010	12.5%	1/9
Between 1 October 1986 to 30 June 1989	10.0%	1/11

158. The tax fraction is found by dividing the tax rate by the sum of 1 plus the tax rate (that is, $r/(1+r)$, where r is the tax rate).

For example, where the tax rate is 15%, the tax fraction is given by $0.15/1.15$. This tax fraction can be simplified to $3/23$ by multiplying both the numerator (0.15) and denominator (1.15) by 20.

Input tax deductions on acquisition or on change in use

159. With regard to timing, a secondhand goods input tax deduction could be claimed by a registered person on the acquisition of goods (subject to payment being made).⁶⁷ However, a deduction could also be claimed later if there has been a change in use of the goods from non-taxable to taxable.⁶⁸ For example, if a person buys a used car for their personal use but later introduces it to their taxable activity. A person could also claim a secondhand goods input tax deduction if they acquired secondhand goods before becoming a registered person and then, on or after becoming a registered person, used the goods for making taxable supplies.⁶⁹ This is illustrated in Example | Tauira 25.

160. The situation is different if before starting a new activity, a person incorporates a company to carry on the activity and then transfers goods to the company. Here there is no change in use by the person because the goods are being transferred to a separate legal entity.

161. In some cases, where goods are acquired on behalf of a company that is yet to be incorporated, the company can be treated as the purchaser of goods in place of the person who acquired the goods on behalf of the company.

162. One way this treatment can arise is under s 22. However, s 22 does not apply where the supply of goods by a person to a company is a taxable supply or is a supply of secondhand goods that is not a taxable supply.⁷⁰

163. Even if a company is not treated as a purchaser, this will not necessarily prevent the company from claiming an input tax deduction, because an input tax deduction may be available in relation to the supply from the person to the company. This is illustrated in Example | Tauira 26.

Example | Tauira 25 – Deduction claimed for asset after registration for GST

Amina acquired a van in 2022 for \$15,000 from an unregistered supplier. She uses the van to collect unwanted furniture, which she restores and sells online. Amina's restoration activity started out as a hobby, but she has widened her activity, and her sales have now grown to the point where she is ready to register for GST.

Amina registers for GST, and in the return covering her first balance date after becoming a registered person claims an input tax deduction for \$1,956.52, being the imputed GST on the purchase price of the van ($3/23 \times \$15,000$). This is on the basis that there has been a 100% change in use from non-taxable to taxable use (because she is now registered).

⁶⁷ Section 20(3).

⁶⁸ Sections 20(3)(e) and 21D(3)(a).

⁶⁹ Sections 20B(1)(a)(iii) and (b).

⁷⁰ Section 22(c).

Example | Taura 26 - Goods acquired by a person on behalf of a company to be incorporated

Brad, who is not registered for GST, has a plan to open a fruit and vegetable shop. Brad's business plan involves the shop being owned and operated by a company, of which Brad will be a director.

Brad works hard to get the shop ready for opening in July 2026.

On 14 June 2026, Brad purchases a secondhand display stand for the shop for \$575 (including GST). He also purchases a new refrigerator for \$2,495 (including GST). Brad keeps receipts for these purchases.

On 8 July 2026, Brad incorporates a company, and on the same day the company reimburses Brad for, among other things, the full cost of the display stand and refrigerator. The company soon after commences trading selling fruit and vegetables.

The company applies to be registered for GST with effect from the date of incorporation and this is approved by the Commissioner. When preparing its return for the two-month period ended 31 August 2026, the company asks whether it can claim an input tax deduction for the purchase of the secondhand display stand and refrigerator.

The company can claim input tax deductions in relation to the secondhand display stand and the new refrigerator.

Section 22 applies to allow the company an input tax deduction of \$325.43 for the new refrigerator. In this case:

- tax was charged under s 8 on the supply of the refrigerator to Brad;
- Brad acquired the refrigerator on behalf of the company;
- Brad became an officer of the company when it was incorporated;
- the company reimbursed Brad in full for the cost of the refrigerator;
- Brad acquired the refrigerator for the purposes of the taxable activity to be carried on by the company;
- Brad has not used the refrigerator for any other purpose;
- the supply of the refrigerator by Brad to the Company is not a taxable supply (Brad is not registered) or a supply of secondhand goods (Brad hasn't used the refrigerator and his ownership does not make the refrigerator secondhand because he did not purchase it for his own use);
- the refrigerator was not acquired more than 6 months before the incorporation of the company; and
- the company (which now has the receipts kept by Brad) holds sufficient records to establish the particulars relating to the deduction to be made.

Section 22 does not apply to the display stand because the supply of the display stand from Brad to the company is a supply of secondhand goods not being a taxable supply (because Brad is not registered for GST). However, the company can still claim a secondhand goods input tax deduction of \$75 ($\$575 \times 3/23$) because the requirements for a secondhand goods input tax deduction are met in relation to the supply from Brad to the company.

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IS 25/23: GST – Meaning of payment

Issued | Tukuna: 11 November 2025

This interpretation statement discusses the meaning of “payment” for GST purposes. The meaning of payment is relevant for determining the time of supply, the tax period for which you return output tax or for which you claim an input tax deduction, and eligibility for a secondhand goods input tax deduction.

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

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- GST: claims for secondhand goods input tax credits on property transactions between associated persons *Tax Information Bulletin* Vol 5, No 11 (April 1994): 1

Summary | Whakarāpopoto

1. This interpretation statement discusses the meaning of “payment” for GST purposes. The meaning of payment is relevant for determining the time of supply, the tax period for which you return output tax or for which you claim an input tax deduction, and eligibility for a secondhand goods input tax deduction. For GST purposes, the following points can be made:
 - A payment can be made with money or by transferring property or providing services (for example, a company could make a payment by issuing shares in itself to a supplier). See from [9].
 - Payment can be made using a promissory note or a bill of exchange. See from [11].
 - Payment is not made if the purchase price for the supply of goods or services is simply deferred or left owing under the supply agreement. See [19].
 - Payment can be made by the purchaser borrowing an amount under a separate loan agreement with the supplier (or another person) and using the amount borrowed to satisfy the payment obligation under the supply agreement. By doing this, payment will be made for GST purposes, even though the purchaser will still owe the supplier an amount under the separate loan agreement. See [20].
 - Payment for a supply could be made by set-off against an existing debt owed by the supplier to the recipient. For example, if the supplier owed the recipient an amount under an existing debt, the amount payable by the recipient for the supply could be offset against the amount owed by the supplier to the recipient. See [25].
 - From an economic perspective there may appear to be no real difference between, for example, an amount left owing under a supply agreement or an amount owing under a separate loan agreement. However, a difference exists for GST purposes. See [30].
 - The GST general anti-avoidance provision (s 76) may apply to arrangements where payment is technically established, but in a way that fails the parliamentary contemplation test. See from [31].
 - Accounting entries can provide at least some evidence that a payment has occurred, but accounting entries may not always be sufficient. The absence of accounting entries does not mean a payment has not been made. However, depending on other evidence available, the timing of the accounting entries could influence the determination of when the payment was made. See [34].
 - The payment of a deposit under an agreement constitutes a payment. See [49].
 - However, where the recipient of a supply makes a payment to a stakeholder, for GST purposes, the recipient has not made, and the supplier has not received, a payment. Payment does not occur until the stakeholder pays the amount to the supplier or is holding the amount only for the benefit of the supplier (that is, when the conditions of the supply contract are satisfied). See from [54]. A supplier can be a stakeholder. See [56].

Introduction | Whakataki

2. We have been asked to clarify the Commissioner's position on the meaning of payment for GST purposes.
3. Whether a payment has been made is relevant in the following contexts:
 - Time of supply. Under s 9(1), the time of supply is the earlier of the time an invoice is issued by the supplier or the recipient, or the time any payment is received by the supplier.
 - The tax period for which you return output tax. For a registered person who accounts for tax on a payments basis,¹ output tax on a supply is generally attributed to a taxable period to the extent that payment for the supply has been received during the period.
 - The taxable period for which you claim an input tax deduction. For a registered person who accounts for tax on a payments basis or a hybrid basis, an input tax deduction is allowed only to the extent that payment has been made.²
 - Secondhand goods input tax deductions. A registered person can make a secondhand goods input tax deduction only to the extent that payment has been made for the goods acquired.³ This applies whether they account for tax on an accruals, payments or hybrid basis.
4. Other guidance on GST and payments (referred to briefly in this statement) is in:
 - **QB 23/06: GST – goods purchased on deferred payment terms;**⁴ and
 - **IS 10/03: GST – time of supply – payments of deposits, including to a stakeholder.**⁵
5. This interpretation statement replaces:
 - **GST: Meaning of payment** *Tax Information Bulletin* Vol 1, No 4 (October 1989): 1.
 - **GST: claims for secondhand goods input tax credits on property transactions between associated persons** *Tax Information Bulletin* Vol 5, No 11 (April 1994): 1.

Analysis | Tātari

Ordinary meaning of payment

6. A payment can be made with money or with the equivalent of money.
7. "Payment" is not defined in the Act. Therefore, payment has its ordinary meaning.
8. In the simplest case, a payment could be made in cash or by transferring money into the supplier's bank account. However, payment can be made in other ways.
9. The dictionary definition of payment suggests that a payment can be made with money or with the equivalent of money. The *Oxford English Dictionary* relevantly defines payment as:⁶
 1. A sum of money (or equivalent) paid or payable, esp. in return for goods or services or in discharge of a debt; wages, pay. ...
 - 2.a. The action or an act of paying money owed; the remuneration of a person with money or its equivalent, in discharge of a debt or in exchange for goods, services, etc.
 - 2.b. The paying of money or its equivalent *for*... goods, services, etc.

¹ Section 19(2).

² Section 20(3)(b)(i).

³ Section 20(3)(a)(ia) and (b)(i).

⁴ QB 23/06: GST – goods purchased on deferred payment terms *Tax Information Bulletin* Vol 35, No 6 (July 2023): 291.

⁵ IS 10/03: GST – time of supply – payments of deposits, including to a stakeholder *Tax Information Bulletin* Vol 22, No 6 (July 2010): 7.

⁶ *Oxford English Dictionary* (online, accessed on 19 June 2025).

10. Case law has also held that payment can be in something other than money. In *Re Mataura Motors Ltd*, the Court of Appeal stated:⁷

... **the word “payment”** in itself is one which in an appropriate context **may cover many ways of discharging obligations** (*White v Elmdene Estates Ltd* [1960] 1 QB 1, 16; [1959] 2 All ER 605, 610, per Lord Evershed MR).

... the question of whether payment has been made **is not entirely dependent on the physical passing of cash** or a cheque.
[Emphasis added]

Promissory note or bill of exchange

11. Payment for a supply can be made using a promissory note⁸ or a bill of exchange.⁹ These instruments, when provided in return for a supply of goods, discharge the payment obligation under the supply agreement and set up a separate payment obligation under the instruments themselves. By providing one of these instruments in return for a supply of goods, payment will no longer be required under the supply agreement; a payment obligation will exist only under the separate instrument.
12. A mere acknowledgment of debt does not constitute payment. If an instrument merely acknowledges the existence of a debt arising under a purchase agreement it is not possible to say that the payment obligation under the purchase agreement has been discharged. This is illustrated in Example | Tauira 2.
13. Whether a document is a promissory note, bill of exchange or mere acknowledgment of debt depends on whether the documents satisfy the relevant definitions, rather than what the document might be called.
14. Although not directly on point, the view that payment can be made using a promissory note or bill of exchange is also consistent with the definition of “money” in s 2, which includes a promissory note or bill of exchange.
15. However, for a promissory note to constitute payment, the promissory note must be genuine. The Commissioner may consider the application of the GST general anti-avoidance provision (s 76) if the supply is between associated persons and, for example, no realistic prospect exists of the recipient making payment under the promissory note. Section 76 is discussed further from [31].
16. The use of promissory notes is illustrated in Example | Tauira 1, Example | Tauira 2 and Example | Tauira 3.

Example | Tauira 1 – Promissory note as payment

Mikaela’s Garage Ltd enters into an agreement with Car Parts Are Us Ltd to purchase \$20,000 of specialised car parts, which need to be imported from overseas. Payment is due on 20 November 2025. Mikaela’s Garage Ltd is registered for GST on a payments basis.

The purchase agreement requires Mikaela’s Garage Ltd to pay for the parts before taking possession. However, Mikaela’s Garage Ltd is unable to make the payment on the due date.

After some negotiation, Car Parts Are Us Ltd agrees to accept a promissory note from Mikaela’s Garage Ltd with payment to be made on or before 20 February 2026.

Mikaela gets some help and on 23 November 2025 prepares and delivers to Car Parts Are Us Ltd the following:

Deed of acknowledgement of debt

I, Mikaela Burns, director of Mikaela’s Garage Ltd, hereby acknowledge that Mikaela’s Garage Ltd is indebted to Car Parts Are Us Ltd in the sum of \$20,000 and Mikaela’s Garage Ltd promises to pay Car Parts Are Us Ltd \$20,000 on or before 20 February 2026.

⁷ *Re Mataura Motors Ltd* [1981] 1 NZLR 289 at 292.

⁸ A promissory note is defined in s 84 of the Bills of Exchange Act 1908 as an unconditional promise in writing made by one person to another, signed by the maker, engaging to pay on demand, or at a fixed or determinable future time, a sum certain in money to or to the order of a specified person or to bearer.

⁹ A bill of exchange is defined in s 3 of the Bills of Exchange Act 1908 as “an unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand, or at a fixed or determinable future time, a sum certain in money to or to the order of a specified person, or to bearer”. A bank cheque, when they were still available, was an example of a bill of exchange. See *Laws of New Zealand Bills of exchange, cheques, and promissory notes* (LexisNexis, online ed, accessed 13 May 2025).

Despite being titled “Deed of acknowledgement of debt”, this is a valid promissory note. It constitutes payment because it discharges the payment obligation under the supply agreement.

In this case, payment under the supply agreement is achieved on 23 November 2025. Among other things, this means that Mikaela’s Garage Ltd is able to claim an input tax deduction in the GST period ended 30 November 2025 for the \$20,000 of specialised car parts purchased.

Example | Tauria 2 – Transfer of property to trust

Cameron, who is not registered for GST, has inherited a holiday home from his father. His father had acquired the holiday home from a non-associated person in 2012 for \$460,000.

Cameron decides to sell the holiday home to Thiseldome Ltd in its capacity as trustee of a trust settled by Cameron. The purchase price for the holiday home is \$1 million. Settlement for the sale and purchase agreement is on 6 July 2026. On settlement, Thiseldome Ltd issues an acknowledgement of debt to Cameron, which refers to the sale and purchase agreement and states:

I acknowledge that Thiseldome Ltd owes Cameron \$1 million and that this is payable on demand.

The following month when Thiseldome Ltd’s accountant is provided with the details of the sale and purchase agreement and the acknowledgement of debt, she points out that the acknowledgement of debt did not achieve payment for the supply. As a result, on 15 August 2026, a new acknowledgement of debt is prepared, which again refers to the sale and purchase agreement and states:

Thiseldome Ltd promises to pay to Cameron \$1 million on demand.

Thiseldome Ltd is registered for GST on an invoice basis and files two-monthly returns. It owns other holiday homes in the area and carries on a taxable activity of holiday home rental. It intends to use the holiday home acquired from Cameron in this activity as well.

Thiseldome Ltd is able to claim a \$60,000¹⁰ secondhand goods input tax deduction on the purchase of the holiday home in its GST return for the period ended 30 September 2026. The first acknowledgement of debt did not achieve payment for the purposes of the secondhand goods input tax deduction. It merely acknowledged the amount that was still payable under the sale and purchase agreement. However, on 15 August 2026 payment was achieved under the second acknowledgement of debt (which constitutes a promissory note despite being called an acknowledgement of debt). The second acknowledgement of debt discharged the payment obligation under the sale and purchase agreement and set up a separate payment obligation.

Variation – different payment schedule

Instead of promising to pay \$1 million on demand under the second acknowledgement of debt, Thiseldome Ltd promises to pay \$50,000 a year to Cameron for the next nine years and the balance (\$550,000) in 10 years’ time.

The result is the same. The acknowledgement of debt still discharges the payment obligation under the sale and purchase agreement. The different repayment schedule under the acknowledgement of debt does not make any difference.

¹⁰ Under s 3A(3BB), the secondhand goods input tax deduction is limited to the tax fraction of the purchase price of the goods when they were last supplied by a person who is not associated with the supplier (Cameron). This means that the deduction is limited to the tax fraction of the purchase price paid by Cameron’s father, that is, $\$460,000 \times \frac{3}{23} = \$60,000$. Section 3A(3BB) applies because Thiseldome Ltd is associated with Cameron (s 2A(1)(g) – trustee/settlor) and Cameron was associated with his father (s 2A(1)(c)(i) – blood relationship).

Example | Taura 3 - Promissory note used in tax avoidance arrangement

Thomas, who is not registered for GST, owns a secondhand luxury car that he acquired new three years ago for \$800,000.

Thomas sells the car to a trust for \$500,000 (which is also the current market value). Thomas is a trustee and a beneficiary of the trust. On the same day, the trustees give Thomas a promissory note promising to pay Thomas \$500,000 on demand.

The trustees are registered for GST. Thomas states that the trustees have acquired the car solely for use in a taxable activity of delivering online food orders.

The trustees do not have any significant funds or assets other than the luxury car they now own. They also do not have any other income earning activity.

The trustees claim a \$65,217.39 secondhand goods input tax deduction on the purchase of the car.

The trustees argue that they have made payment for the car using the promissory note and are otherwise eligible for a secondhand goods input tax deduction.

In this case, the Commissioner might consider the application of the anti-avoidance provision in s 76 (discussed further from [31]). One of the concerns here is that the payment obligation under the promissory note may never be satisfied. This is because the food delivery activity is unlikely to generate enough profit to repay the loan principal and the trustees have no other significant funds, assets or income earning activity. There may also be concerns relating to private use of the vehicle and whether a taxable activity will eventuate. Further, there may be concerns if the arrangement involved a plan by Thomas to forgive the loan or settle money on the trust that would allow the trustees to repay the loan.

Payment by transferring property or providing services

17. Payment for the supply of goods or services could be made by transferring property or by providing services, as in a barter transaction.¹¹
18. This is illustrated in Example | Taura 4.

Example | Taura 4 – Payment by issuing shares in company

Ranjna, who is not registered for GST, owns land that is suitable for a warehouse development. Ranjna agrees to sell the land to Dhillon Warehousing Ltd (DWL) for \$3 million. DWL is registered for GST and files GST returns monthly.

DWL pays Ranjna a cash deposit of \$300,000 when the agreement for sale and purchase is entered into on 1 April 2026.

Settlement takes place on 1 June 2026. On this date, a further cash payment of \$700,000 is made. DWL also issues shares worth \$2 million to Ranjna, which Ranjna accepts in part payment of the purchase price.

In this case, the deposit of \$300,000 is paid by DWL and received by Ranjna on 1 April 2026. On these facts, there is no indication that the deposit is received by Ranjna in the capacity as a stakeholder.¹²

The cash payment of \$700,000 is paid on settlement date.

The issue of shares is also a payment made on settlement date. The issue or transfer of shares is a common form of non-monetary payment.

11 In *White v Elmdene Estates* [1959] 2 All ER 605 (CA) at 610, Lord Evershed MR concluded that the word payment may cover many ways of discharging obligation, including a payment in kind. See also *Case T61* (1998) 18 NZTC 8,461 (TRA) where it was held that the recipient of a supply had made a payment by issuing shares to the supplier. In that case, the issue of the shares was subject to the supplier having a put option that allowed them to sell the shares back to the recipient after a certain date. The supplier attempted to exercise the put option, but the recipient was unable to comply and subsequently filed for bankruptcy. The supplier omitted the share component of the sale price from their return arguing that the issue of the shares did not constitute payment. The Taxation Review Authority held the issue of shares constituted payment by way of barter.

12 Payments to stakeholders are discussed from [52].

Assuming other requirements are met, DWL may be able to claim a secondhand goods input tax deduction. However, a secondhand goods input tax deduction is available for a period only to the extent that payment has been made in the period.¹³ In this example, this means that DWL is able to claim secondhand goods input tax deductions of \$39,130.43 (\$300,000 x 3/23) in the return for the period ended 30 April 2026 and \$352,173.91 (\$2,700,000 x 3/23) in the return for the period ended 30 June 2026.

Payment using an amount borrowed under a separate loan agreement

19. Payment will not be made if the purchase price for the supply of goods or services is simply deferred or left owing under the supply agreement.¹⁴
20. However, payment can be made by the purchaser borrowing an amount under a separate loan agreement with the supplier (or another person) and using the amount borrowed to satisfy the payment obligation under the supply agreement. By doing this, payment will be made for GST purposes, even though the purchaser will still owe the supplier an amount under the separate loan agreement.
21. In *Nicholls*, Tipping J noted that the taxpayer in that case could have made payment by way of an external or vendor mortgage.¹⁵ He stated at [30]:¹⁶

... If he had settled the transaction in full when title became available, funding the purchase by way of an external or indeed a vendor mortgage, he would thereby have made payment of the whole balance and would have been entitled to an input tax credit on that basis.
22. A similar decision was made in *Faith Construction*.¹⁷ In that case, a law change was announced that was to apply to certain supplies from 1 June 1984. In light of the announcement, the taxpayers in that case, who had existing building contracts with customers, entered into arrangements with their customers for payment by the customers to occur before 1 June 1984, which would avoid the application of the law change. In the case of two of the taxpayers, the arrangements involved payment by the customers with the condition that the building company would immediately lend back to the customers equivalent sums. The loans to the customers were to be repaid progressively as architects' certificates for work done were obtained. In the case of the other two taxpayers, the arrangements involved the payments being paid into a deposit account, only to be released for the company's use on the receipt of the architects' certificates. The Court of Appeal held that payment had been made under the supply agreements, notwithstanding the loans back to the customers or the conditions on the payments into the deposit account. The liability of the customers to pay under the supply contracts was discharged.
23. Bingham LJ concluded that there was a full upfront payment to the builder for the building work, despite the loan back, stating at 920:

There is of course much law as to what in the absence of agreement amounts to payment, but in the contractual context my understanding is that A pays the price to B when he does that which B agrees to accept as payment of the price.
24. This is illustrated in Example | Tauira 5.

¹³ Or in the relevant earlier period if a deduction is claimed in accordance with the proviso in s 20(3).

¹⁴ *Case U31* (2000) 19 NZTC 9,293 (TRA).

¹⁵ *Nicholls v CIR* (1999) 19 NZTC 15,233 (CA). The important point is that there is separate loan agreement. It is not important that the loan is secured by a mortgage, for example.

¹⁶ See also *Case S99* (1996) 17 NZTC 7,622 (TRA) where it was held that payment was made when the recipient provided the supplier with an unconditional and irrevocable letter of credit from the recipient's bank, despite the letter of credit having a payment date six months in the future. A letter of credit from a third party constitutes a payment where it satisfies the recipient's payment obligations under the supply agreement and the supplier agrees to rely solely on the letter of credit to receive payment. See also *Re Mataura Motors Ltd* where a debenture was issued in satisfaction of a payment obligation; and *Case Q10* (1993) 15 NZTC 5,061 (TRA) where a payment was made when a taxpayer agreed to receive payment over time secured by a mortgage over property.

¹⁷ *Customs and Excise Commissioners v Faith Construction Ltd* [1990] 1 QB 905 (CA).

Example | Taura 5 - Payment with funds from separate loan agreement

Owen who is not registered for GST, owns shares in a courier company. On 30 March 2026, Owen sells a van that he owns in his own name to the company for \$15,000. The company intends to use the van as a courier vehicle.

There is no payment of cash or bank transfer, but there is a loan agreement between Owen and the company under which Owen agrees to lend the \$15,000 purchase price to the company. Company resolutions note the purchase of the van by the company from Owen and the loan made by Owen for the purchase price of the van. A credit entry is made in the company accounts "30 March 2026, Shareholder Loan – Owen, \$15,000".

The company wants to know whether it can claim a secondhand goods input tax for the taxable period ended 31 March 2026.

The company can claim a secondhand goods input tax deduction. There has been a payment of \$15,000 in the taxable period ended 31 March 2026. A separate loan agreement has been entered into that has discharged the payment obligation for the sale of the van. The secondhand goods input tax deduction may be limited if Owen owns enough shares to be associated with the company.¹⁸

Payment by set-off against existing debt

25. Payment for a supply could be made by set-off against an existing debt.
26. For example, if the supplier owed the recipient an amount under an existing debt, the amount payable by the recipient for the supply could be offset against the amount owed by the supplier to the recipient.
27. In *Healing Industries*, the High Court stated:¹⁹

In the taxation context, the issue was considered by the Federal Court of Australia in *Whim Creek Consolidated NL v FC of T* 77 ATC 4,503. The taxpayer had lent money to a subsidiary. Subsequently, the subsidiary allotted shares to the taxpayer as fully paid. The amount payable on the allotment was set off against the advances received from the taxpayer. The Federal Court held that **the monies set off against the monies due on allotment were "monies paid on shares"** for the purposes of the relevant taxing provision.

What in my view emerges from these and other cases is that **in appropriate circumstances it can properly be held that a payment has been made by the release of a financial obligation or by the discharging of a contractual obligation**. I can see no reason why this general approach should not apply in these circumstances. The premium was the difference between the par value and the market value of the Healing shares transferred to the Avery Wood shareholders. The "payment" for that premium was effected by the transfer of the Avery Wood shares by the Avery Wood shareholders to Healing. The value of the Avery Wood shares is fixed by the agreement of the 15th December 1980 at the purchase price set out therein of \$3,875,000. Part of the value of those shares was the consideration that passed for the premium portion of the value of the Healing shares. I am left in no doubt that any man of business would regard that premium as having been "paid" by the Avery Wood shares transferred to Healing. [Emphasis added]

28. See also *Case L34*²⁰, discussed at [37].
29. Payment by offsetting existing debt is illustrated in Example | Taura 6.

¹⁸ See IS 25/22 – Secondhand goods input tax deduction.

¹⁹ *Healing Industries Ltd v CIR* (1988) 10 NZTC 5,115 at 5,118.

²⁰ *Case L34* (1989) 11 NZTC 1,204 (TRA).

Example | Taura 6 – Payment by offsetting existing debt

Scott is registered for GST on the payments basis. Scott is a builder and has an account with Sharpest Edge Ltd for tool maintenance services. Scott owes \$2,500 on his account.

Sharpest Edge Ltd has a workshop doorframe that needs fixing. Scott offers to take care of the doorframe for \$250. Sharpest Edge Ltd agrees and reduces the amount owing on Scott's account by \$250. On the same day, Sharpest Edge Ltd emails Scott an updated statement showing "3 December 2025, Payment (Thank you!) – services provided, \$250 credit, balance \$2,250".

Although there was no exchange of cash or bank transfer, Sharpest Edge Ltd has made a payment for Scott's services by offsetting the amount of the fee against the amount Scott owes on his account. Therefore, Scott will need to return GST for fixing the doorframe in his two-monthly GST return for the period ended 31 January 2026.

At the same time, Scott has made a \$250 payment on his account for tool maintenance services. This means he will be able to claim input tax on the payment in the period ended 31 January 2026.

Not an economic equivalence approach

30. From an economic perspective there may appear to be no real difference between, for example, an amount left owing under a supply agreement or an amount owing under a separate loan agreement. However, a difference exists for GST purposes. Whether a payment has been made for GST purposes depends on the legal effect of the transactions entered into. This was discussed in *Nicholls*, where the Court of Appeal stated at [32]:

As I understand him Mr Nicholls also argued that, in spite of the transaction being structured as a deferred payment, rather than as full settlement with a vendor mortgage, the Court should treat the transaction according to its general effect. It was suggested that the transaction should be treated as if there had been an exchange of cheques or the conveyancing equivalent. It is sufficient to say that this did not happen. The Court cannot proceed as if the transaction had been structured differently, or as if it had been carried out differently, on some sort of economic equivalence basis. **Tax is payable or not and deductions are allowable or not, in accordance with the legal consequences of the transaction into which the parties have entered, not upon the basis of what they might have done to achieve the same outcome.** [Emphasis added]

Anti-avoidance

31. The GST general anti-avoidance provision (s 76) may apply to arrangements where payment is technically established, but in a way that fails the parliamentary contemplation test.²¹ This is illustrated in Example | Taura 3.
32. *Glenharrow* provides an example.²² In that case, a non-registered person supplied a mining licence to the taxpayer (who was registered) for \$45 million. Except for an \$80,000 deposit, payment was made by way of vendor finance. The Supreme Court accepted the taxpayer's argument that the vendor finance technically constituted payment for the purposes of the secondhand goods input tax deduction requirement. However, despite technical compliance with the input tax provision, the Supreme Court held that the arrangement was a tax avoidance arrangement, so was void for GST purposes.
33. The Supreme Court considered the size of the company purchaser, the company's lack of capitalisation or backing from its shareholder, the shrinking value of the mining licence and the mining licence's very limited practical life. On an objective view, the court found that the effect of the structure was to produce a GST refund totally disproportionate to the economic burden undertaken by the purchaser or the economic benefit obtained by the vendor from the vendor finance. On the facts in *Glenharrow*, the payment for the supply was artificial because realistically the purchaser could not repay the \$45 million vendor finance.

Accounting entries as evidence of a payment

34. Accounting entries can provide at least some evidence that a payment has occurred. However, accounting entries may not always be sufficient.
35. This is because whether a payment has been made depends on the legal effect of the transactions that have been entered into. The legal effect may not be clear solely from the accounting entries and more evidence may be needed (for example, a separate loan agreement or a clear company resolution). For example, an accounting entry simply showing an amount

²¹ The parliamentary contemplation test is discussed in IS 23/01 Tax avoidance and the interpretation of the general anti-avoidance provisions sections BG 1 and GA 1 of the Income Tax Act 2007 *Tax Information Bulletin* Vol 35, No 2 (March 2023): 8. Although IS 23/01 primarily relates to the Income Tax Act 2007, it is also relevant to the s 76.

²² *Glenharrow Holdings Ltd v CIR* [2008] NZSC 116.

owing from a recipient to a supplier could reflect either a separate loan agreement used to pay for a supply or a situation where part of the purchase price has merely been left owing under the supply agreement (without a separate loan agreement).

36. The burden of proving that payment under the supply agreement has occurred is on the registered person. It may be difficult for the registered person to satisfy this burden if they are relying solely on accounting entries.
37. In *Case L34*,²³ the Taxation Review Authority considered whether payment was made through accounting entries. It also illustrates how a payment can be made by set-off against existing debt (see from [25]), so it is useful to describe the facts in some detail here.
38. In *Case L34*, incoming shareholders subscribed for shares in a company. The incoming shareholders paid for the shares using amounts lent to them by the company's principal shareholder. The loan from the principal shareholder to the incoming shareholders was reflected in entries made to the current accounts the shareholders had with the company. The entries included a debit to the principal shareholder's current account (which reduced a separate debt owed by the company to the principal shareholder) and corresponding credit entries to the current accounts of the incoming shareholders. This essentially transferred credit with the company from the principal shareholder to the incoming shareholders. Debit entries were then made to the current accounts of the incoming shareholders to pay for their share subscriptions. In that case, the parties to the dispute accepted that the book entries reflected loans from the principal shareholder to the incoming shareholders.
39. The Taxation Review Authority held that a payment may be made by accounting or book entries only, if the entries relate to a genuine transaction. However, the authority also noted that it is not good practice to merely rely on book entries. The authority stated at 1,212:

In my view, there is no doubt that "payment" is wider than the mere transferring of cash. **Accounting entries which cause crediting in account, by debiting to another account, amount to "payment". A payment may be made in a number of forms and by means other than a physical transfer of cash.** I am in no doubt that payments of subscriptions for shares may be made in non-cash forms. **Payments may be made by accounting or book entries only, if bona fide in relation to a genuine transaction.** I am satisfied that the procedures followed by the company and the objectors did amount to a "payment" in respect of the shares subscribed for by the objectors. **Those accounting entries reflected genuine commitments between the parties.** However, **I do not think it is good practice to merely rely on book entries to record non-cash transactions.** Professional advisers usually require formal agreements or some sort of documentation or, at least, a careful series of company resolutions. [Emphasis added]

40. The absence of accounting entries does not mean a payment has not been made. Funds borrowed under a separate loan agreement could be legally set off against a payment obligation under a supply agreement. This would result in a payment under the supply agreement – even if accounting entries to reflect this are not made until later. However, depending on other evidence available, the timing of the accounting entries could influence the determination of when the payment was made.
41. The relevance of accounting entries was also discussed in *Case K60*:²⁴

The resolution purported to divide the amount of the tax free dividend in issue, \$23,375, among the shareholders of the company by declaring it to be credited to their current accounts. **It seems to me that any book entry or accounting thereafter would be no more than evidence** of the performance of the resolution by the directors. As in the case of realisation, so in the case of the type of distribution being considered, **I do not think it is necessary for an actual cash payment to be made or a book entry to be made** evidencing such or a transfer of interest in the capital sum, for it to be a "transaction", if not also a "payment". [Emphasis added]
42. The relevance of accounting entries is illustrated in Example | Tauria 7 and Example | Tauria 8.

²³ *Case L34* (1989) 11 NZTC 1,204.

²⁴ *Case K60* (1988) 10 NZTC 487 (TRA) at 494-495.

Example | Tauria 7 – Transferring assets to a new company

Camila has been carrying on a taxable activity in her own name for the last two years but has decided it is time to incorporate a company, Churros by Camila Ltd, to carry on the activity. Camila owns 100% of the shares in the company.

On 5 May 2026, Camila sells her churro making equipment to the company for \$2,000. The company is registered for GST on a payments basis.

The company has no cash yet, so no cash payment could be made for the equipment.

However, the following journal entries are made in the company's accounts:

Assets

5/05/2026 Equipment \$2,000 debit

Liabilities**Shareholder current account – Camila**

5/05/2026 Loan - equipment \$2,000 credit

Camila wants to know whether the company, which is registered for GST on a payments basis, can claim an input tax deduction for the equipment.

Accounting entries can provide at least some evidence that a payment has occurred, but accounting entries may not always be sufficient.

In this case, other than the reference in the accounting entry to a "loan", no evidence exists of a loan entered into. There is also no suggestion that the purchase price obligation has been set off against an amount owing by Camila to the company (like in *Case L34*).

The burden of proving that a payment has been made is on the company. In these circumstances, the company has not satisfied the onus of proving that there is a separate loan agreement and, therefore, that a payment has been made. Therefore, the company cannot claim an input tax deduction yet.

Example | Tauria 8 – Proving a separate loan agreement was entered into

Abida runs school holiday music programmes and is registered for GST on a payments basis.

On 28 November 2025, Abida purchases instruments from Soulful Sounds for \$1,500 (including GST) for a holiday programme she intends to run in January and February 2026. Abida pays Soulful Sounds \$750 on 28 November, and Soulful Sounds agrees to take the remaining \$750 in February once Abida has run her holiday programme.

Soulful Sounds records the following entry in its accounts: "28 November 2025, Rising Stars loan scheme – Abida, \$750 debit.

Abida claims an input tax deduction for the full \$1,500 in her return for the two months ended 30 November 2025.

Inland Revenue reviews Abida's return for the period ending 30 November 2025. Inland Revenue requests bank statement information from Abida and other information from Soulful Sounds relating to transactions with Abida. Inland Revenue notices that Abida has claimed a deduction for \$1,500 despite only paying \$750 in the period. There is no evidence of any discussion between Abida and Soulful Sounds in November 2025 about a loan. As part of the review, Soulful Sounds accounting records, including the entry above, are obtained as they relate to Abida. Soulful Sounds also provides Inland Revenue with information it received from its accountant when it first set up its Rising Stars loan scheme. The advice noted that one of the advantages of the scheme (other than encouraging music education) was that purchasers who accounted for GST on the payments basis could claim deductions upfront.

After the GST review has started, Abida and Soulful Sounds provide a completed Rising Stars loan programme application. The form has been recently completed but is backdated to 28 November 2025.

Although Soulful Sounds has a loan scheme and has recorded the debt as a loan in its accounts, there is little objective evidence that Soulful Sounds and Abida actually entered into a separate loan agreement or even discussed the nature of the amount left to pay in November 2025. Little (if any) weight is likely to be placed on the recently completed application form.

The burden of proving there was a separate loan agreement is on Abida. On the evidence available, there is a risk that Inland Revenue will not accept the existence of the loan and will propose an adjustment to her return to deny part of deduction claimed. In the absence of a separate loan agreement, it appears that Abida has paid only \$750 in the period ended 30 November 2025.

Abida would have been in a better position to satisfy her burden of proof if she and Soulful Sounds had completed a Rising Stars loan programme application at the time of purchase.

If part of the deduction is disallowed in the period ended 30 November 2025, Abida would be able to claim it in the period ended 31 March 2026, assuming she pays the remaining \$750 in that period.

Deferred payment

43. Specific deferred payment scenarios are considered in QB 23/06: GST – goods purchased on deferred payment terms.²⁵ QB 23/06 considered four types of agreement and provided guidance as summarised in Table | Tūtohi 1:

Table | Tūtohi 1 Deferred payment

Summary – for payments basis persons	
Type of agreement	When an input tax deduction can be claimed
Standard sales agreement	When and to the extent that payment has been made.
‘Buy now, pay later’ (BNPL) agreement	Typically, when the agreement is entered into as the BNPL provider pays for the supply in full.
Hire purchase agreement	When the agreement is entered into.
Layby sales agreement	When property in the goods is transferred, typically after final payment has been made.

44. As stated at [19] of this interpretation statement, payment will not be made if the purchase price of the supply of goods or services is simply deferred or left owing under the supply agreement. Store credit accounts are an example of a standard sales agreement offering deferred payment terms.
45. As discussed at [20], payment can be made by the purchaser borrowing an amount under a separate loan agreement with the supplier (or another person) and using the amount borrowed to satisfy the payment obligation under the supply agreement. By doing this, payment will be made for GST purposes, even though the purchaser will still owe the supplier an amount under the separate loan agreement. Buy now, pay later (BNPL) agreements are an example of this. Under BNPL agreements, payment is typically made at the time the supply and the BNPL agreements are entered into. This is because the BNPL provider has paid for the goods or services in full, and the recipient of the supply has entered into a separate agreement with the BNPL provider.
46. Specific time of supply rules apply in the case of hire purchase agreement²⁶ and layby sales agreements.²⁷
47. Where goods and services are supplied under a hire purchase agreement, the supply is deemed to take place at the time the agreement is entered into (even though payment has not been made under the hire purchase agreement).

25 QB 23/06: GST – goods purchased on deferred payment terms *Tax Information Bulletin* Vol 35, No 6 (July 2023).

26 Section 9(3)(b).

27 Section 9(2)(c).

48. Where goods and services are supplied under a layby sales agreement, the supply occurs when property in the goods is transferred, typically after final payment has been made.

A deposit is a payment

49. The Commissioner's view is that the payment of a deposit under a supply agreement constitutes a payment for the supply. This applies equally to conditional and unconditional contracts.²⁸
50. An alternative view, not accepted by the Commissioner, is that a deposit does not constitute a payment until the supply agreement has been completed. This alternative view is based on the idea that a deposit's primary purpose is as a guarantee or surety provided by the purchaser. However, the Commissioner considers that a purpose of a deposit is also to provide a part payment of the purchase price.
51. This is discussed further in IS 10/03: GST – time of supply – payments of deposits, including to a stakeholder.²⁹ IS 10/03 also discusses payments to stakeholders.

When a payment is made to a stakeholder

52. Sometimes a payment for a supply is made to a person to hold until a condition of the supply contract is satisfied. A person who receives such a payment is commonly called a stakeholder.
53. For example, where a deposit is paid to a real estate agent for the purchase of land, the real estate agent may hold the deposit for the parties as a stakeholder. A stakeholder generally holds the amount in a contractual or quasi-contractual capacity for the supplier and recipient, not as agent for the supplier.
54. Where the recipient of a supply makes a payment to such a stakeholder, for GST purposes, the recipient has not made, and the supplier has not received, a payment. Therefore, assuming no invoice has been issued, the time of supply is not triggered for the supply.³⁰
55. For GST purposes, the recipient does not make, and the supplier does not receive, the payment unless and until the stakeholder pays the amount to the supplier or is holding the amount only for the benefit of the supplier.³¹ For example, once an agreement becomes unconditional and the stakeholder's obligations are at an end, the amount is held for the supplier's benefit and the payment is received by the supplier from that point in time.
56. A supplier can be a stakeholder.³² Where a payment is made to a supplier in their capacity as stakeholder, for GST purposes payment will not occur until they receive a beneficial interest in the payment (that is, when the conditions of the supply contract are satisfied).

28 A conditional contract refers to a binding contract that is subject to conditions, as opposed to a case where conditions exist that must be satisfied before there will be a binding contract.

29 IS 10/03: GST – time of supply - payments of deposits, including to a stakeholder *Tax Information Bulletin* Vol 22, No 6 (July 2010): 7.

30 Section 9(1).

31 IS 10/03 at [44].

32 IS 10/03 and *CIR v Dormer* (1997) 18 NZTC 13,446 (HC).

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Bills of Exchange Act 1908, ss 3, 84

Goods and Services Tax Act 1985, ss 9, 19, 20, 76.

Income Tax Act 2007

Case references | Tohutoro kēhi

Case K60 (1988) 10 NZTC 487 (TRA)

Case L34 (1989) 11 NZTC 1,204 (TRA)

Case Q10 (1993) 15 NZTC 5,061 (TRA)

Case S99 (1996) 17 NZTC 7,622 (TRA)

Case T61 (1998) 18 NZTC 8,461 (TRA)

Case U31 (2000) 19 NZTC 9,293 (TRA)

CIR v Dormer (1997) 18 NZTC 13,446 (HC)

Customs and Excise Commissioners v Faith Construction Ltd [1990] 1 QB 905 (CA)

Glenharrow Holdings Ltd v CIR [2008] NZSC 116

Healing Industries Ltd v CIR (1988) 10 NZTC 5,115 (HC)

Mataura Motors Ltd, Re [1981] 1 NZLR 289 (CA)

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IS 25/24: Income tax and GST – industries other than forestry registered in the Emissions Trading Scheme

Issued | Tukuna: 11 November 2025

This interpretation statement applies to industries registered in the Emissions Trading Scheme, other than forestry which is taxed differently. The industries include those that are emissions intensive and trade exposed, as well as those involved in removal activities and some horticultural activities. The statement sets out the conceptual framework for the income tax treatment of emission liabilities and emissions units (NZUs) in these sectors. It then explains how to calculate deductions for emission liabilities and it discusses the treatment of NZUs as income. Finally, there is a brief discussion of the GST treatment of NZUs.

For a discussion on forestry activities registered in the ETS see: **IS 25/13: Income Tax and GST – forestry activities registered in the Emissions Trading Scheme.**

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

Key terms used in this statement

- 1. The following terms are used in this statement when considering how the Emissions Trading Scheme (ETS) applies to industrial activities.

Term	Meaning in this statement
allocation	An allocation of NZUs given to a business that has eligible industrial activities that are considered EITE or that is undertaking removal activities.
Climate Change Response Act 2002 (CCRA)	The Act that provides a framework by which New Zealand is developing and implementing climate change policies to enable New Zealand to meet its international obligations under the United Nations Framework Convention on Climate Change, the Kyoto Protocol and the Paris Agreement; and provides for the implementation, operation and administration of a greenhouse gas emissions trading scheme in New Zealand that supports and encourages global efforts to reduce the emission of greenhouse gases.
eligible emitter	A business that is making greenhouse gas emissions and that is eligible for industrial allocation because they are EITE.
emission intensive and trade exposed (EITE)	Industries that require a lot of power to support their production and that cannot pass on to customers the increased costs of the ETS they incur due to competition from mainly offshore suppliers that may have different or weaker ETS equivalents.
emissions	The release of greenhouse gases and/or their precursors into the atmosphere over a specified area and period.
emissions liability	The obligation on emitters to transfer NZUs to the surrender account to match their annual emissions.
Emissions Trading Scheme (ETS)	The greenhouse gas emissions trading scheme established under the CCRA.
entitlement	NZUs that a voluntary participant in the ETS may earn for removal activities under sch 4 of the CCRA provided they submit an emissions return.
Environmental Protection Authority (EPA)	The authority established under the Environmental Protection Authority Act 2011 that runs the ETS.

Term	Meaning in this statement
greenhouse gas	Carbon dioxide, methane, nitrous oxide, any hydrofluorocarbon, any perfluorocarbon, and sulphur hexafluoride.
industrial allocation	The provision of free NZUs to emitting industries considered to be EITE.
industries/industrial activity	Industries registered in the ETS other than forestry and including industries that have emissions that are required to be registered; industries without emissions that are affected by ETS costs; and industries carrying out greenhouse gas removal activities that can choose to register. Forestry activities in the ETS have a different tax regime and are covered in IS: 25/13 Income Tax and GST – forestry activities registered in the Emissions Trading Scheme .
NZU	A unit as defined in s 4(1) of the CCRA approved as a New Zealand unit by the Registrar. The NZU is the domestic unit created for the ETS. One NZU corresponds to one metric tonne of carbon dioxide–equivalent emissions.
participant	A person who is required to or chooses to register in the ETS.
provisional allocation	An initial entitlement to NZUs for eligible industrial activities under s 81 of the CCRA calculated by reference to production in the preceding emissions year
removals	A removal activity listed in part 2 of sch 4 of the CCRA and involving carbon dioxide–equivalent greenhouse gases that are either removed from the atmosphere or not released into the atmosphere, or a reduction from reported emissions.
surrender	The transfer of NZUs to the Crown surrender account to meet an emissions obligation.
synthetic greenhouse gas (SGG)	A hydrofluorocarbon, perfluorocarbon or sulphur hexafluoride.

Introduction | Whakataki

- Emissions trading is a tool to encourage and enable the reduction of greenhouse gas emissions that contribute to climate change. The ETS is a market the Government manages with the objective of getting long-lived gases linked to climate change to net zero by 2050. The ETS covers about half of all emissions in New Zealand, including those from fossil fuels, industrial processes and waste. Participation in the ETS can either be mandatory or voluntary depending on the type of activity being carried out.
- Participants in the ETS that generate greenhouse gases need to surrender one NZU for each whole tonne of carbon emissions from their relevant activities.¹ The number of NZUs available to the market reduces over time, which is expected to cause prices to rise, incentivising participants to find ways to reduce their emissions. Participants can decide whether to cut their own emissions or effectively pay others to reduce emissions by buying NZUs.
- NZUs can be bought at government auctions or from other market participants, including from forestry and others who earn NZUs for carbon removal. NZUs may also be provided to certain industries for free under a method known as industrial allocation and to businesses that remove or destroy greenhouse gases.
- This statement considers the income tax and GST issues that arise for participants in the ETS other than those in the forestry sector. Income tax and GST issues for forestry participants in the ETS are considered in **IS 25/13: Income Tax and GST – forestry activities registered in the Emissions Trading Scheme**.

¹ Section 63 of the Climate Change Response Act 2002 (CCRA).

6. For general information on the ETS, see:
 - Environment Protection Agency, [Emissions Trading Scheme](#)
 - Ministry for the Environment, [New Zealand Emissions Trading Scheme](#)
 - C Leining, [A Guide to the New Zealand Emissions Trading Scheme: 2022 update](#).

How the ETS applies to industrial activities

7. This statement focuses on participants that generate greenhouse gas emissions and incur a liability to surrender NZUs to match their annual emissions. It also covers the tax treatment of free NZUs issued to participants as a form of subsidy from the Government or because their activities reduce emissions.
8. Recipients of free NZUs may or may not have emissions liabilities. Industries with emissions liabilities that are regarded as both emission intensive and trade exposed (EITE), are allocated free NZUs annually as a subsidy. The free NZUs are allocated based on production levels to incentivise the EITE businesses not to relocate offshore. Free NZUs can also be allocated to businesses that reduce or destroy gases that adversely affect the ozone layer, that may have no surrender obligations.
9. Some parties are obliged to report their annual emissions but are not required to meet emissions liabilities, such as parts of the agriculture sector. Other industries such as liquid fuel importers have both mandatory reporting and liabilities to satisfy under the ETS. Parties who are not obliged to report or surrender NZUs may elect to be in the ETS and then earn free NZUs if their activities reduce emissions or global warming.
10. Given this diversity, the non-forestry industries in the ETS and the removal activities that are eligible to receive NZUs are set out in the Appendix.
11. Before considering the tax issues, the statement considers how industrial allocation operates to provide free NZUs to EITE industries.

Industrial allocation

12. Industrial allocation is the provision of free NZUs to industries considered EITE. Industrial allocation reduces the cost impact of the New Zealand ETS for EITE industry with the purpose of reducing competitive disadvantages with offshore businesses subject to weaker climate policy. International differences in climate policy could otherwise drive the production of EITE businesses and the associated emissions overseas, increasing global emissions and undermining New Zealand's commitment to reduce these.
13. Businesses undertaking 26 different industrial activities are eligible for industrial allocation. They include:
 - aluminium smelting
 - cement
 - burnt lime (calcium oxide)
 - steel
 - cut roses
 - methanol
 - newsprint and tissue paper
 - cucumbers.
14. Industrial allocation is based on the annual level of production, the emissions intensity for the particular activity determined by fixed allocative baselines, and the level of assistance determined from time to time. This reflects the extent to which emissions costs are met by industrial allocation as determined by an eligibility test based on emissions per million dollars of revenue.
15. Emitters must file an ETS return for the annual emissions year (starting 1 January and ending 31 December) by 31 March the following year with their production for that prior emissions year. At any time from 1 January to 30 April, eligible emitters can apply for an industrial allocation based on their prior year's production. The industrial allocation is provisionally allocated in May. Eligible emitters' final allocation is determined under s 83 of the Climate Change Response Act 2002 (CCRA) based on their actual production figures for the emissions year ended 31 December. The provisional allocation is then deducted from the final allocation to determine their annual allocation adjustment (that is, the shortfall or excess number of free NZUs for the relevant emissions year).

- 16. If the final allocation of free NZUs exceeds the provisional allocation, additional free NZUs are provided in May the following year. If the final allocation is less than the provisional allocation, the excess free NZUs can either be offset against the provisional allocation made for the next emissions year in May that year, or be returned to the Crown, again by May.
- 17. As all these activities take place contemporaneously in May, the net free NZUs (after all adjustments) are credited to eligible emitters at one time.
- 18. An eligible emitter who is applying for an industrial allocation for the first time does not receive a provisional allocation in their first emissions year as they have not filed an emissions return with their production figures for the prior emissions year. They just receive the final allocation after filing their production figures for their first emissions year and thereafter adopt the process set out above.
- 19. Detail about industries in the ETS and their obligations, which can be mandatory or elective, depending on their emissions and activity, is in the Appendix.

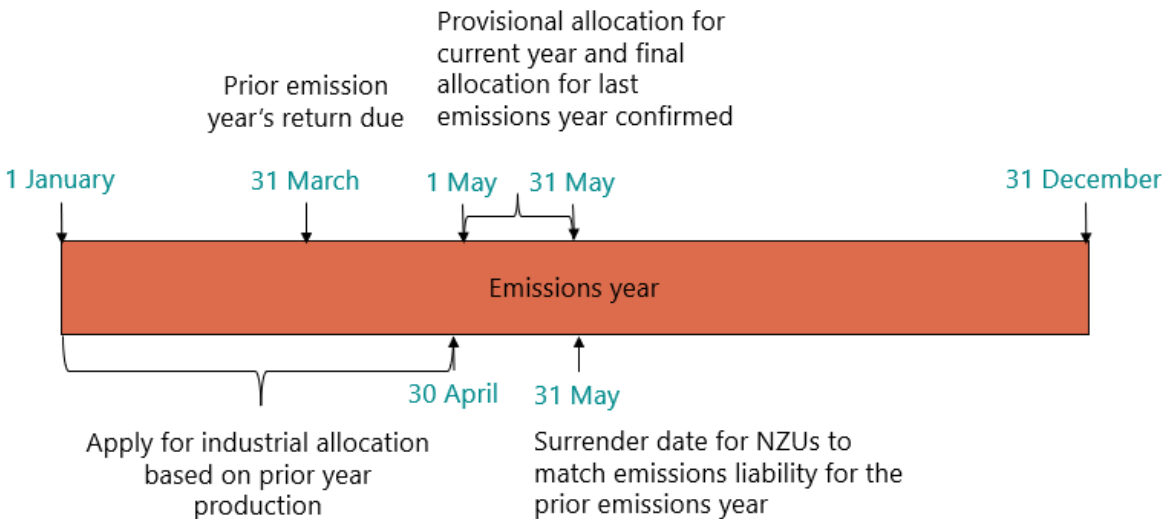
Allocation of free NZUs for removal activities

- 20. Removal businesses that elect into the ETS receive a final allocation of free NZUs in May after filing an annual (or quarterly) return setting out the greenhouse gases they have removed for the emissions year. These businesses are entitled to receive one NZU for each whole tonne of removals they make.
- 21. For details of removal activities eligible to receive free NZUs, see the Appendix.

Timeline of key emissions dates

- 22. The following are key dates in an emissions year as shown in Figure | Hoahoa 1:
 - 1 January – 31 December – Emissions year
 - 31 March – prior emissions year’s return due
 - 1 January – 30 April – apply for industrial allocation based on prior year production
 - 1 May – 31 May – provisional allocation for current emissions year and allocation adjustment based on final allocation for last emissions year
 - 31 May – last date to surrender NZUs to match emissions liability

Figure | Hoahoa 1: Diagram of the key dates in an emissions year



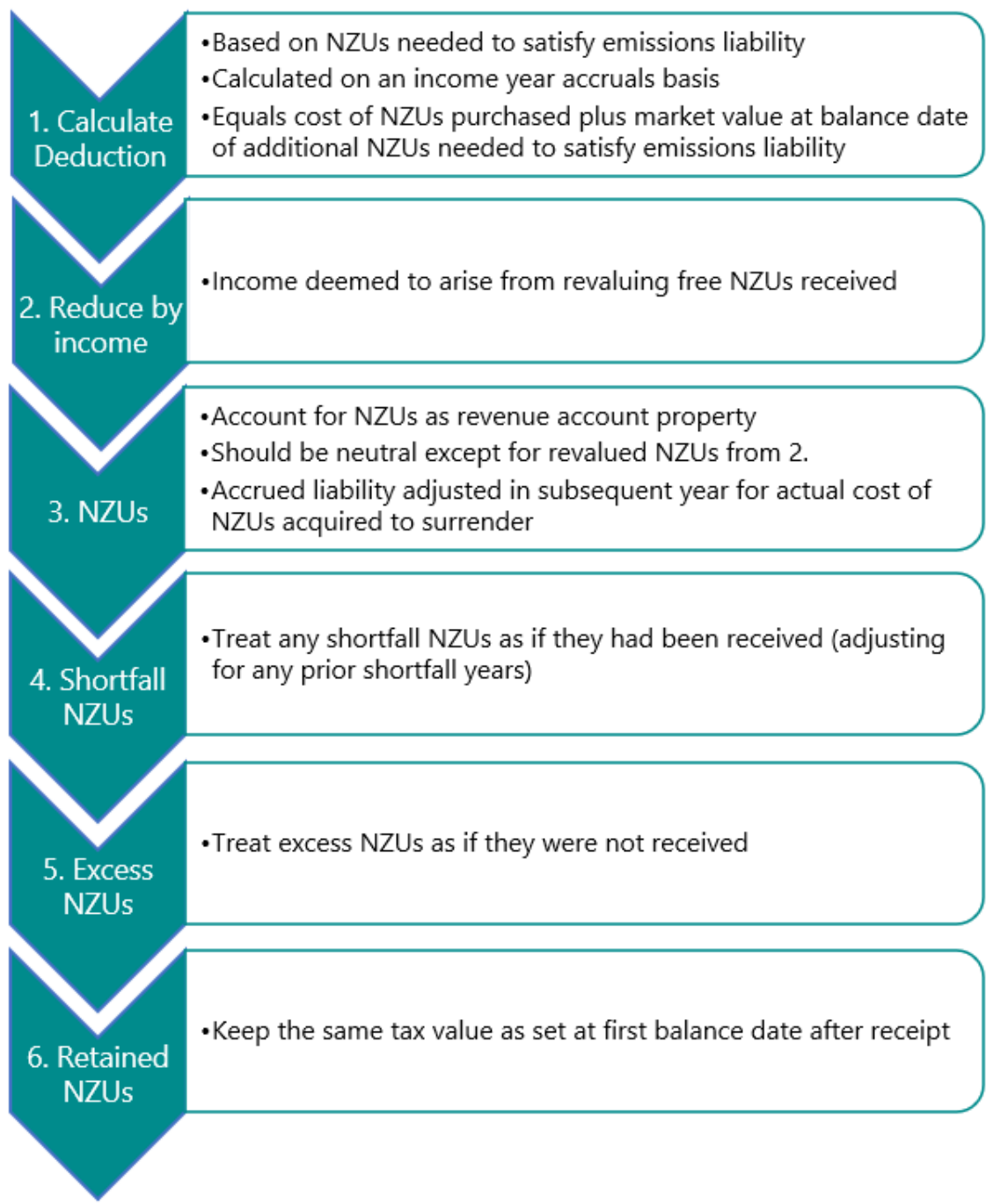
Conceptual scheme for the taxation of industrial activity in the ETS

23. The conceptual scheme for taxing industrial participants in the ETS needs to be understood before discussing the legislation in detail. This summary of the ETS provides a framework against which the more detailed analysis can be viewed. The summary covers:
- the overarching scheme (from [24]);
 - calculating deductions for emissions liabilities (from [32]);
 - accounting for NZUs as revenue account property (from [44]); and
 - shortfalls and excess free NZUs (from [75]).

Overarching scheme

24. The conceptual scheme for taxing these participants in the ETS is relatively straightforward. Businesses are allowed a deduction for the emissions liabilities they incur. The emissions liabilities are determined by the number of NZUs required to be surrendered based on production amounts. This is done on an accrual basis, using ordinary accounting principles and general tax provisions.
25. NZUs are treated as revenue account property and rules apply similar to those for trading stock. This means there are valuation provisions that apply when NZUs are acquired and again at balance date, with opening values being a deduction and closing values treated as income. Any NZUs acquired in the open market retain their initial cost price. Disposals of NZUs give rise to assessable income and a disposal not only includes NZUs sold but also those surrendered.
26. However, it gets complicated when a business receives free NZUs. Instead of reducing the deduction for the emissions liability on the basis that the business did not “incur” that liability (because it received free NZUs), the value prescribed for the free NZUs produces income that offsets the excess deduction.
27. Further complications arise where there is a shortfall or excess in the number of free NZUs provided. This typically arises because of the process of a provisional allocation of free NZUs followed a year later by a final allocation. These shortfalls or excesses need to be included or excluded to determine the correct position on an accrual basis.
28. Complexity also arises when the income year balance date of a business does not align with the calendar year that applies for an emissions year. This frequently demands the inclusion of the emissions liabilities and the allocation of NZUs relating to the parts of two different emissions years that fall into the business’s income year.
29. If a business retains free NZUs at balance date it must value them to market value at the first balance date after receipt and treat this as income. Then they continue to use this same market value at any subsequent balance date that the same free NZUs are still held, until such time as they are disposed of or surrendered.
30. The overarching scheme is summarised in Figure | Hoahoa 2.

Figure | Hoahoa 2: Overarching scheme for taxing industrial allocation in the ETS



Worked examples

31. This statement proceeds step-by-step through the issues using an ongoing worked example. Example | Tauria 1 sets out the relevant background facts for the worked example and these facts apply on through the subsequent examples

Example | Tauira 1 – Hexxus Ltd's background facts

Hexxus Ltd is an EITE business and is required to participate in the ETS.

Hexxus Ltd's relevant dates are as follows:

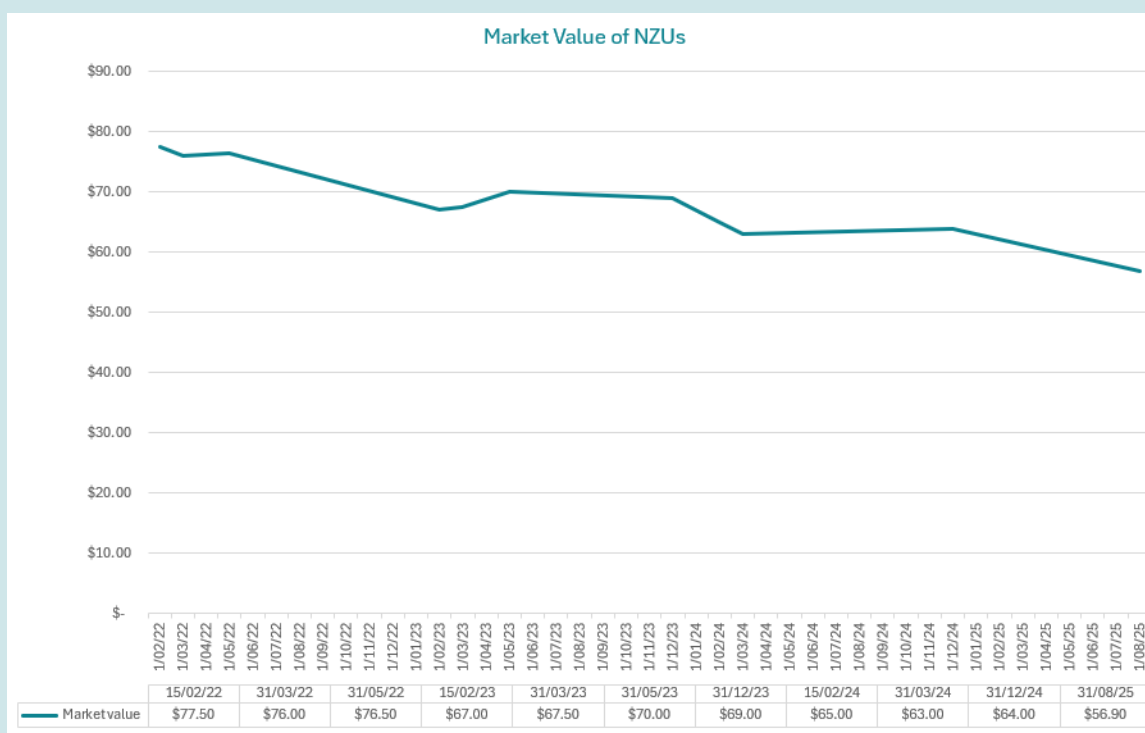
- **1 January 2023:** start of 2023 emissions year and first date for filing the 2022 emissions return
- **31 March 2023:** end of the 2023 income year and last date for filing the emissions return for the 2022 emissions year
- **31 May 2023:** date by which NZUs must be surrendered for the 2022 emissions year
- **31 December 2023:** end of 2023 emissions year

Hexxus Ltd is liable to surrender NZUs to satisfy its emissions liabilities and because of its EITE status it receives free NZUs.

This worked example makes various assumptions, to better illustrate how ETS taxation works conceptually, that may not reflect the reality of most emitting businesses:

- Hexxus Ltd's emissions years before and including 2022 have no shortfall or excess of free NZUs. The facts are varied from Example | Tauira 4 onwards to illustrate a shortfall and later an excess of free NZUs.
- NZU allocation, surrender and prior year adjustments are all done at the same time in May each year.
- All emissions are based on production which is consistent and known for each quarter, so the emissions liability is known with certainty at the end of each quarter.
- The spot price for NZUs at the various dates used in the examples below are shown in Figure | Hoahoa 3 (figures are intended to be indicative and may not be the actual market value on the day).

Figure | Hoahoa 3: Market value of NZUs



Hexxus Ltd is focused on reducing its emissions over time and its allocative baseline for industrial allocation has been reducing over this period as it changed to renewable energy sources. This meant its provisional allocation of free NZUs was reducing each year and not just reflecting the prior year's productions levels. Its emissions liabilities for each of the 2022-2024 emissions years are shown in Figure | Hoahoa 4:

Figure | Hoahoa 4: Emissions liability and free unit allocations

Emissions year (calendar year)	Emissions liability in NZUs	Prov allocation of NZUs	Final allocation of NZUs
2022	520	300	300*
2023	480	280	260
2024	400	200	220

* This is the final allocation under the example as stated. Note that there is a variation of the example in Example | Tauria 4 where a shortfall exists, and the final allocation increases to 320 NZUs.

Hexxus Ltd received 300 free NZUs for the 2022 emissions year and is required to purchase the balance needed to satisfy its emissions liability.

Hexxus Ltd bought 220 NZUs in February 2023 for \$67 per NZU.²

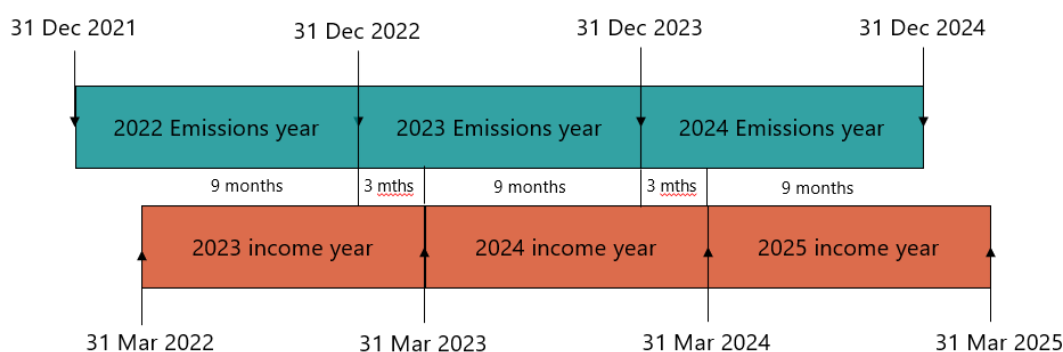
Deductions for emissions liabilities

32. Participants in the ETS that have emissions are required to surrender one NZU for each whole tonne of carbon emissions from their relevant activities. Emitters (other than foresters) can claim a deduction for these emission liabilities.
33. There are no specific deduction provisions for emissions liabilities outside the forestry sector. Deductions for emissions liabilities of all other emitters are available under ordinary principles, using the general permission, s DA 1. The approach to deductibility of emissions liabilities follows the financial reporting accrual method by permitting a deduction for the actual or expected liabilities for the emissions years to the extent those liabilities fall into the relevant income year. Where a deduction is claimed based on an expected liability, this should be reversed and replaced by the actual liability in the subsequent year.

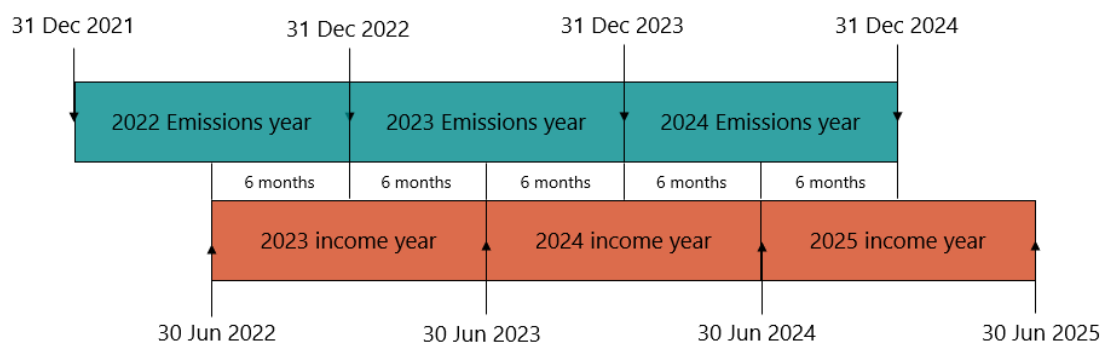
Determining the emissions liability

34. Surrender of the relevant number of NZUs to meet the emissions liability must occur by 31 May following the end of each emissions year. Therefore, the first step is to determine the number of NZUs required to be surrendered for the income year on an accrual basis.
35. For an emitter with an income year balance date of 31 March for example (participants should use their own balance date), they can deduct:
 - 9 months of the liability to surrender NZUs for the past emissions year ending the preceding 31 December ie from 1 April to 31 December; and
 - 3 months of their expected liability to surrender NZUs for the current emissions year that started on 1 January through to 31 March.
36. The overlap of emissions years and income years is illustrated in Figure | Hoahoa 5.

² For the purposes of the worked example, NZU values may not reflect actual NZU values at any particular point in time.

Figure | Hoahoa 5: The overlap between emissions years and income years for standard balance dates

37. As at 31 March, the emitter will know the actual NZU surrender obligation for the 9 months of the past emissions year, as they will have filed their emissions return by that date. The emissions return sets out their production output over the period from which their emissions liability and consequent surrender obligation can be determined.
38. For the 3-month period from 1 January, the emitter will have details of their actual production output so can calculate their actual liability for this part period of the current emissions year. Similarly, if an emitter has a June balance date, the overlap periods will all be 6-month periods as shown in Figure | Hoahoa 6.

Figure | Hoahoa 6: The overlap between emissions years and income years for June balance dates

Calculating the amount of the emissions liability deduction

39. Calculating the amount of the emissions liability deduction involves several steps. The first step is to determine the emissions liability on an accrual basis as noted above from [334]. This gives an amount of NZUs required to be surrendered. The second step is to work out how to quantify the liability to surrender NZUs in monetary terms. This involves understanding how the NZU emissions liability will be satisfied. Generally, an emitter will use its free NZUs first and purchase additional NZUs to make up the balance of the emissions liability.
40. For NZUs purchased during the income year, a deduction is available at cost to the extent there is a liability to surrender that number of NZUs in that income year. The cost of these NZUs must be determined using at the business's choice: either the first in first out (FIFO) or weighted average cost (WAC) valuation methods for valuation purposes under s ED 1(5). Other methods may be available if the business has an exemption from using GAAP for financial reporting and a record is kept of the reason for departing from FIFO or WAC.
41. The value of any additional NZUs that will be required to meet the surrender liability for the income year over and above those purchased can be deducted by calculating the required number of additional NZUs at the market value (NZU spot price) at balance date. Any variance between the market value at balance date of those additional NZUs and their actual cost when acquired post balance date, that are used to meet the surrender liability, should be brought to account in the following income year following normal accounting principles.

42. The calculation of the emissions liability ignores:
- the extent to which free NZUs are allocated to the business;
 - any expenditure or loss relating to the acquisition of free NZUs (s DB 60); and
 - NZUs surrendered during the income year (these surrenders result in income under s CB 36 as a result of being treated as deemed sales at given values –discussed at [54]).
43. Example | Tauira 2 explains how to calculate a deduction for an emissions liability.

Example | Tauira 2 – Hexxus Ltd’s emissions liability for the 2023 income year

Hexxus Ltd’s emissions liability deduction for 31 March 2023 is based on the liability that it accrues by producing emissions and incurring obligations to surrender NZUs over the two emissions years which fall into the period up to balance date.

Step 1 – determine the number of NZUs required to surrender

Hexxus Ltd needs to calculate the number of NZUs that it must surrender for the emissions it produced for the income year ended 31 March 2023. A calculation is required because Hexxus Ltd’s income year (31 March) does not line up with the emissions year (31 December).

Hexxus Ltd’s emissions liability deduction is based on:

- Liability for the period 1 April 2022 – 31 December 2022 in the 2022 emissions year; and
- Liability for the period 1 January 2023 – 1 April 2023 in the 2023 emissions year.

Hexxus Ltd’s total emissions liability for the 2022 emissions year was 520 NZUs (from Example | Tauira 1). The emissions liability from 1 April 2022 to 31 December 2022 is 9/12ths of 520, which is 390 NZUs.

Based on its improved emissions figures, Hexxus Ltd calculates that it has a liability of 120 NZUs for the period from 1 January 2023 to 31 March 2023.

Hexxus Ltd has a total emissions liability deduction for the income year ending 31 March 2023 based on 510 NZUs (390 + 120) as shown in Figure | Hoahoa 7:

Figure | Hoahoa 7: Emissions years liabilities accrued to income years

Emissions year (ending 31 December)	Total emissions liability in NZUs	Emissions liability 1 Jan to 31 Mar	Emissions liability 1 Apr to 31 Dec	Income year accrual (ending 31 March)
2022	520	130	390	
2023	480	120	360	510
2024	400	100	300	460
2025		95		395

So, for the 2022 emissions year (ending 31 December 2022), Hexxus Ltd needs to surrender 520 NZUs in May 2023, but after accrual accounting for the 2023 income year (ending 31 March 2023), for tax purposes Hexxus Ltd has a liability to surrender 510 NZUs for that income year.

Step 2 – calculate the deduction

Having worked out the number of NZUs that Hexxus Ltd is required to surrender for the 2023 income year (510 NZUs), the second step is to determine the value of those NZUs. This is done by using the actual cost of any NZUs that Hexxus Ltd purchased and valuing the balance using the market value at balance date of the additional NZUs required to satisfy the emissions liability. Therefore, the deduction under s DA 1 for the emissions liability in the 2023 income year comprises two amounts:

- the cost of NZUs that Hexxus Ltd purchased to meet the liability; and
- the value of the balance of further NZUs required to meet the liability.

Hexxus Ltd had purchased 220 NZUs at \$67 per NZU in February 2023 (totalling \$14,740). Therefore, Hexxus Ltd can deduct \$14,740 for the cost of purchased NZUs.

Hexxus Ltd can also deduct a further amount for the value of the 290 NZUs it is definitively committed to surrender. This deduction ignores the free NZUs received as its provisional allocation. Hexxus Ltd values the liability to surrender a further 290 NZUs at the market value of \$67.50 at 31 March 2023, being \$19,575.

Hexxus Ltd's total deduction for emission liabilities for the 2023 income year is:

$$\$14,740 + \$19,575 = \$34,315$$

Variation on the facts – NZUs purchased post-balance date

Under this variation on the facts, Hexxus Ltd does not purchase any additional NZUs prior to balance date. Hexxus Ltd decides to defer the purchase of the NZUs until closer to 31 May 2023 when it will need to surrender them.

The effect of not purchasing any NZU's before balance date is that the whole deduction is calculated based on the market value of the number of NZUs required to meet the emissions liability. This means Hexxus Ltd's deduction is \$34,425.00, being 510 NZUs at the market value of \$67.50 at 31 March 2023.

When the 220 additional NZUs are purchased in the next income year, closer to the surrender date of 31 May, any variance between the market value at the prior year end and the actual cost must be brought to account in that income year.

In May 2023, Hexxus Ltd purchases the 220 NZUs it needs to surrender on 31 May 2023 at \$70 each. As a result, Hexxus Ltd calculates there is an additional \$550.00 (being $220 \times \$2.50$ – the difference between the \$70 cost and the \$67.50 market value at balance date) deduction it can claim in the 2024 income year.

Accounting for NZUs as revenue account property

44. The previous analysis and example focused on the deduction available for an emissions liability. However, as noted in the conceptual framework, that deduction is overstated because the business does not **incur** that full liability to surrender that quantity of NZUs because it is eligible to receive free NZUs under the ETS. Instead of reducing the deduction by the free NZUs received, the Act effectively cancels some of the deduction by treating NZUs as revenue account property like trading stock and revaluing them to market value at year end.
45. NZUs are classed as excepted financial arrangements under s EW 5(3B) and "revenue account property" under s YA 1. They are treated in a similar manner to trading stock for tax purposes with the closing value at the end of the year treated as income under s CH 1 and the opening value at the beginning of the year (being the same as the closing value the prior year) deductible under s DB 49. The valuation provisions for this purpose are in subpart ED.
46. Where an NZU has been purchased, its value at year end is its cost under s ED 1(1). Costs are allocated by choosing either the FIFO or WAC method under s ED 1(5).
47. Free NZUs allocated for industrial allocation or removal activities have their own valuation provisions in ss ED 1B and ED 1(7B). These provisions determine values when free NZUs are first allocated to the person and then at tax balance date.
48. The way in which these sections operate is complex (because they need to accommodate the process of provisional allocation of free NZUs in May each year and a subsequent adjustment to that allocation after the final allocation is determined in May the following year). The provisions also allow for the complexity that arises when a business has a tax balance date that does not align with the emissions year ending on 31 December with a consequent need to accrue parts of two emissions years into one income year.

Valuation of free NZUs

49. The tax value of free NZUs must be considered:
- on initial allocation when free NZUs are transferred to the participant;
 - at balance date; and
 - on disposal either by surrender to meet an emissions liability or by sale.
50. While ordinarily it might make sense to address these chronologically, the rules relating to disposal of the NZUs are straightforward and it is necessary to understand them when accounting for NZUs at balance date. Therefore, the value of free NZUs on disposal is considered first.

Value of NZUs on disposal

51. As noted in [49], a disposal of NZUs occurs both when they are surrendered to satisfy an emissions liability and when they are sold.

Disposal of NZUs by way of sale

52. Under s CB 36(2), disposal of NZUs by way of sale gives rise to assessable income for the vendor at the sale price. A deduction is available under:
- s DB 49(4) for the original cost if the NZUs were purchased in a prior income year and the value at the end of the prior income year for free NZUs and
 - the general permission, s DA 1, if they were acquired in the same income year.
53. Where the NZU sold was transferred to a participant as a free NZU and is still valued at zero when sold, no deduction is available as s DB 60(2) denies it.

Disposal of NZUs by surrender

54. NZUs surrendered to meet an emissions liability under the CCRA are treated as a sale to unrelated parties. The surrendered NZUs are treated by s CB 36(3) as having been sold at:
- Market value on the surrender date where the NZU was valued at zero on receipt and remains valued at zero when surrendered.
 - The value determined at year end if the free NZU was previously revalued at the end of an income year under s ED 1B.
55. If neither of the above applies and the NZU was purchased, its cost is the deemed disposal value on surrender.

Value of free NZUs on initial allocation

56. Section ED 1B sets the values for free NZUs where the free NZUs have been held continuously by that person from the time of original transfer to them.³
57. These free NZUs are valued at zero at the time of original transfer by s ED 1B(2) provided there is no unit shortfall in an earlier income year.
58. However, if the business has a unit shortfall from a prior income year, the free NZUs are allocated the market value applying at the end of each prior shortfall income year (s ED 1B(3) and (4)). Allocation to prior shortfall income years occurs until the shortfall for each income year (oldest first) is satisfied. Usually this will be only the prior income year. Any remaining surplus of free NZUs received over the shortfall amount is allocated a zero value at initial allocation. This is discussed in more detail from [75].

Value of free NZUs at balance date

No unit shortfall in prior income year

59. Subsections (5) to (8) of s ED 1B set out the value to be applied to free NZUs at balance date where there is no unit shortfall in a prior year and where any shortfall from prior years has been cleared. As noted at [57], most free NZUs are going to be valued at zero on receipt.
60. The free NZUs on hand at balance date are valued at market value on balance date up to the level of the free NZU entitlement for the income year. Any free NZUs exceeding that entitlement for the income year remain valued at zero.

3 Section ED 1B applies to free NZUs transferred for industrial allocation, for removal activity and by public authorities for negotiated greenhouse agreements (supplementary agreements and rebates for indirect emissions charges).

61. The free NZU entitlement is determined in the same way as the emissions liability. For a March balance date business, the emissions liability is determined by accruing the 9-month and 3-month periods from the successive emissions years to determine the correct amount for the income year (see Figure | Hoahoa 5). For the free NZU entitlement⁴, the same calculation is done.
62. The maximum number of free NZUs revalued to market at balance date is determined by the formula in s ED 1B(6) using the definitions in s ED 1B(7), provided the amount is never less than zero:
Unit entitlement - disposals at zero value
63. The maximum number of free NZUs revalued to market value at balance date is the “unit entitlement” for the income year (ie, for a March balance date business, the 9 months and 3 months of the successive emissions years), less any disposals made during the income year when the value of the disposed free NZUs was zero. The formula takes into account the business’s final entitlement to free NZUs for the parts of the emissions years that are accrued into the income year, if it is a recipient of an industrial allocation and the allocation entitlement if it is receiving free NZUs for removal activity.
64. A business with a 31 March balance date will know its final unit entitlement for the past emissions year, as the return for this must be filed by 31 March. The business will also know its production or removal figures for the 3 months of the current emissions year, so can calculate its correct entitlement for the part period (even though it would not yet be finalised).
65. Only three types of free NZUs might be valued at zero on disposal.
 - Free NZUs valued at zero on receipt and disposed of (including surrendered) before balance date. Provided they are disposed of before balance date, s ED 1B(8) will not apply to revalue them to market value.
 - Free NZUs that are valued at zero under s ED 1B(8)(b). For s ED 1B(8)(b) to apply, there needs to be an excess number of free NZUs because of a final allocation that is less than the related provisional allocation. Those excess NZUs are then valued at zero at balance date and carried forward at that value. Excess NZUs are discussed from [90].
 - An excess number of free NZUs could also arise where a business with a balance date such as 30 June, has received a provisional allocation in May but only has to account for 50% of this (ie for the period 1 January to 30 June) at balance date as it is not a “unit entitlement” which is defined on an income year basis.
66. It is important to note that the definition of “disposals at zero value” in s ED 1B(7)(b) refers to NZUs that had a **value** of zero at disposal. The **value** at disposal can be different from any **income** deemed to arise on disposal. Section CB 36 treats a surrender of a NZU as a deemed sale at a given value and treats all disposals as income. It does not, however, alter the NZU’s tax **value** at the time of disposal. Therefore, for example, if a free NZU has a **value** of zero at the time of surrender it will be included in the formula in s ED 1B(6) as a disposal at zero value even if it is treated as a sale at market value under s CB 36(7).
67. Any free NZUs that exceed the number determined by the formula are valued at zero under s ED 1B(8)(b).
68. Accounting for the values of the NZUs held by a business is illustrated in Example | Tauira 3.

Example | Tauira 3 – Accounting for the NZUs held in the 2023 income year

This example builds on Example | Tauira 2 where the NZUs purchased were bought in February 2023 and not the variation where they were purchased post-balance date. The focus is on the NZUs that Hexxus Ltd acquired, held and disposed of during the income year. This is similar to accounting for trading stock.

Where it potentially differs is through the accruals that are required at balance date. Because the income year may not line up with the emissions year, various accruals are required to include the correct amount of NZUs in the income year. As a consequence, the correct accrual of NZUs may be different from the actual number of NZUs on hand at any point in time.

This example is intended to show how to account for the NZUs across the 31 March 2023 balance date. In order to have the correct figures for the income year ending 31 March 2023, the same accruals will need to have been done for the income year ending 31 March 2022. At this point in the example, the accruals for the 2022 income year will be ignored to focus on the accruals for the 2023 income year.

⁴ Because an industrial allocation is production-based with a baseline determined by different industry emission profiles and the amount of the entitlement is being gradually reduced and adjusted over time, the level of assistance frequently changes from emissions year to emissions year.

Free NZUs

For the 2021 emissions year the final allocation of free NZUs for Hexxus Ltd was confirmed at 340 NZUs, the same as provisionally received in May 2021. As a result, no allocation adjustment was received in May 2022.⁵ The provisional allocation for the 2022 emissions year was 300 NZUs and received in May 2022. Once again, the final allocation matched the provisional allocation for the 2022 emissions year. However, Hexxus Ltd's provisional allocation for the 2023 emissions year received in May 2023 was reduced to 280 NZUs as they commenced their transition to totally renewable energy sources and the baseline was adjusted accordingly. These NZUs have a value of \$0 on receipt (s ED 1B(2)).

Hexxus Ltd's final allocation of NZUs for the 2023 emissions year was reduced further to 260 NZUs. When calculating the accruals for an income year from an emissions year, it is important to use the final allocation and not the provisional allocation. This will be an instance where the accrual for tax purposes differs from the amount of NZUs physically on hand. This was summarised in Figure | Hoahoa 4.

Free NZUs equal to the unit entitlements for the parts of the 2022 ($300 \times 75\% = 225$) and 2023 ($260 \times 25\% = 65$) emissions years that fall into the income year ended 31 March 2023 must be valued at market value on 31 March 2023 ($225 + 65 = 290 \times \$67.50 = \$19,575.00$) as they are part of the unit entitlement for the income year (s ED 1B(8)(a)). The value of the NZUs on hand is income as closing stock (s CH 1(4)). The same value is then deductible the next year as opening stock (s DB 49(4)).

Figure | Hoahoa 8: Summary of accruals of final allocations of free NZUs

Income year ending	31/03/2022	31/03/2023	31/03/2024
9 months from previous calendar year	255	225	195
3 months from next calendar year	75	65	55
Final NZUs accrual	330	290	250

Purchased NZUs

The 220 NZUs purchased in February 2023 are valued at their cost (\$67) at balance date (s ED 1(1)). These NZUs remain on hand at the end of the income year because they are not surrendered until 31 May. The value of the NZUs on hand of \$14,740 ($220 \times \67) is income as closing stock (s CH 1(4)). The same amount is then deductible the next year as opening stock (s DB 49(4)).

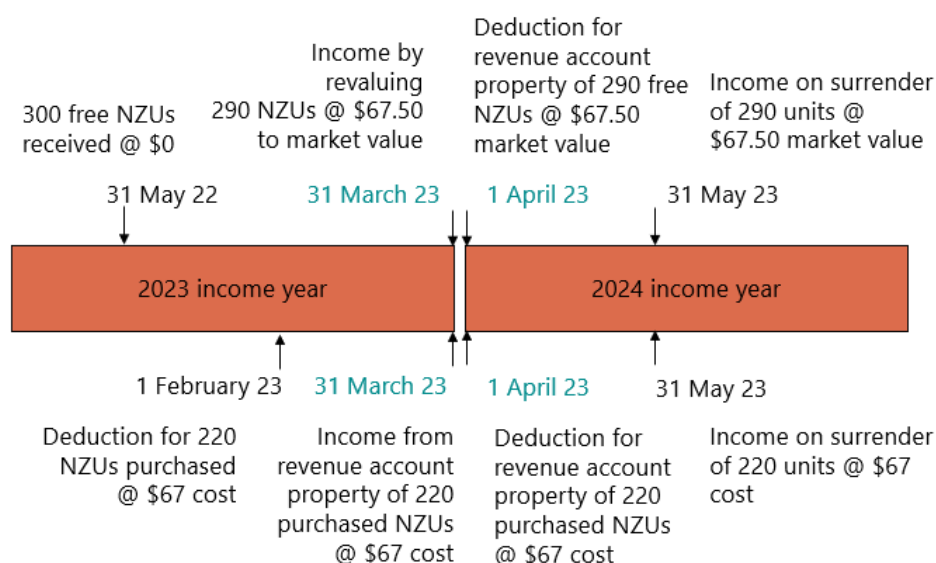
Net position

Under subpart ED, Hexxus Ltd has income of \$19,575 and \$14,740 = \$34,315 in total in relation to the NZUs that are treated as on hand as at 31 March 2023. However, this income is offset by Hexxus Ltd having two deductions relating to the purchase of the 220 NZUs. As explained in Example | Tauira 2, Hexxus Ltd has a deduction of \$34,315 for its emissions liability as at 31 March 2023. This deduction is partially based on the cost of the 220 NZUs (\$14,740). Additionally, Hexxus Ltd has a deduction under s DA 1 for \$14,740 being the actual cost of purchasing the 220 NZUs in February 2023.

⁵ We start the example with no previous shortfall or excess of NZUs to more clearly show how to treat excess and shortfall NZUs. However, we go on to demonstrate how to do this by varying the facts. The reader is encouraged to accept the simple position proposed knowing that the real situation is likely to be more complex.

69. The concepts from Example | Taurira 3 are illustrated in Figure | Hoahoa 9.

Figure | Hoahoa 9: Income and deductions for NZUs at 31 March 2023 balance date



70. As can be seen from the entries along the bottom of Figure | Hoahoa 9, accounting for the 220 purchased NZUs effectively cancels out any tax consequences for the NZUs themselves. A deduction for their cost is obtained on purchase, and they are brought in as closing stock at balance date at the same amount. The cost is then deducted at the start of the 2024 income year as revenue account property, and income of the same amount arises when the NZUs are surrendered in May. This means the purchased NZUs do not give rise to net income or a deduction.
71. It is different for the 300 free NZUs received (shown along the top of Figure | Hoahoa 9). These are received at no cost, but when the 290 NZUs accrued to the 2023 income year are revalued to market value at balance date, the market value of these NZUs becomes income at balance date.
72. However, as noted at [44], this income created from the free NZUs is the mechanism used to reduce the deduction claimed for the emissions liability that is not actually incurred as it is satisfied by the free NZUs.
73. A trading account summarising Hexxus Ltd's NZUs might look like Figure | Hoahoa 10. This shows that the transactions involving NZUs net out, and Hexxus Ltd is left, in an economic sense, claiming a deduction for its emissions liability that it incurred based on the cost of the NZUs it needed to purchase. Figure | Hoahoa 10 also shows the disconnect between the NZUs actually received and those accrued into the 2023 income year. It shows the 300 NZUs received in May but only 290 being revalued to market value at 31 March 2023. The 10 NZUs are the difference between those needed to surrender on 31 May 2023 for the 2022 emissions year (520 NZUs), and the accrued liability of 510 NZUs for the 2023 income year (as explained in Example | Taurira 2). Hexxus Ltd needs to surrender those 10 NZUs for the 2022 emissions year in May 2023 but they were accounted for in the 2022 income year.

Figure | Hoahoa 10 – Hexxus Ltd's 2023 position

Date	Description	Cost or MV	No of NZUs	Income	Deduction
May 2022	Provisional allocation of free NZUs	0.00	300	0	0
February 2023	Purchase of NZUs on market	67.00	220		\$14,740.00
March 2023	Deduction for emissions liability – see Example Tauira 2			0	\$34,315.00
	Revaluation of free NZUs to market value – see Example Tauira 3 (ss ED 1B(8) and CH 1(4))	67.50	290	\$19,575.00	0
	Income under s CH 1(4) for purchased NZUs being revenue account property	67.00	220	\$14,740.00	
	Subtotals			\$34,315.00	\$49,055.00
	Net position				(\$14,740.00)

74. While Figure | Hoahoa 10 shows the accruals for the 2023 income year, this does not reflect the NZUs that Hexxus Ltd physically has on hand. For this reason, many participants will need to keep separate tax accounts to track NZUs in addition to their NZU register details. Assuming (as noted in Example | Tauira 1) that Hexxus Ltd had exactly the number of NZUs required to be surrendered in May 2022, Hexxus Ltd would have had no NZUs on hand prior to receiving its provisional allocation of 300 NZUs in May 2022. In February 2023, Hexxus Ltd bought a further 220 NZUs. This is summarised in Figure | Hoahoa 11:

Figure | Hoahoa 11 – Hexxus Ltd's NZUs on hand

Date	Hexxus Ltd – NZU account	NZUs
31 May 2022	Opening balance	0
31 May 2022	Provisional allocation	300
15 Feb 2023	NZUs purchased	220
31 Mar 2023	Total NZUs	520
31 Mar 2023	Liability to surrender NZUs in May 2023	520

NZU shortfall in prior income year

75. In practice and unlike the 2021 and 2022 emission years in Example | Tauira 3, the reality is that the provisional allocation of NZUs will not match up with the actual entitlement to free NZUs. This means, there will be a shortfall or excess of free NZUs received. Such a shortfall can arise, for example, because the provisional allocation of free NZUs is based on the past year's production and if production in the relevant year is increasing, the final allocation will be a greater amount. Likewise, an excess can arise where production has dropped from the past year (or emissions are reducing) and the final allocation of free NZUs is less than the provisional allocation. The tax treatment where there is an excess of free NZUs is discussed below from [90].

76. Like the other tax calculations, the shortfall is determined on an income year basis, and not on an emissions year basis. Also, the “unit entitlement” definition in s ED 1B(7)(a) reflects the final allocation entitlement for the emissions year not the provisional allocation. When the participant’s balance date is not 31 December, the unit entitlement comprises the pro-rated portions of the final entitlements for two emissions years (as per Figure | Hoahoa 5).
77. The Act has specific rules for treating and valuing free NZUs to ensure the correct amount of income and deductions are returned taking into account these variations between provisional and final allocations. Where the maximum number of free NZUs revalued from zero to market value at balance date under s ED 1B(8)(a), as determined under the formula in s ED 1B(6), is greater than those actually held by the business at balance date, the difference is treated as a unit shortfall under s ED 1B(9).
78. Having a unit shortfall affects (at least) two income years. It affects the year that is a shortfall year and the subsequent income year(s) until the unit shortfall is resolved. This is because for the shortfall year, unit shortfalls are treated as being on hand at balance date and revalued to market value then, even though they will not be received until the next income year when the allocation adjustment is processed in May following the emissions year ending on 31 December.
79. As mentioned, the unit shortfalls are treated as if they were additional NZUs held by the participant under s ED 1B(11) (that is, the same as NZUs on hand) for the purposes of assessing income at year end under s CH 1 and the corresponding deduction at the beginning of the next income year under s DB 49.
80. To ensure the shortfall is not treated as income again when made up in the subsequent income year under the allocation adjustment, s ED 1B(4) assigns the market value of NZUs at the end of the relevant shortfall year (oldest first) to the free NZUs received in that subsequent year until the unit shortfall for that prior year is satisfied. This then reduces the “unit shortfall” and the “unit shortfall value” for that year to zero under s ED 1B(10) and the year ceases to be an “emissions unit shortfall year” (s YA 1).
81. Any further free NZUs the business receives in the subsequent year are then valued in the same manner as NZUs received in an income year that does not follow on from a unit shortfall year under s ED 1B(5) to (8).

Example | Tauira 4 – Emissions unit shortfall year

Hexxus Ltd – variation on the facts

Under this variation to the fact scenario, Hexxus Ltd discovers that its 2023 income year is an “emissions unit shortfall year” as defined in s ED 1B(9).

In March 2023, Hexxus Ltd provides its annual emissions return for 2022, showing it has a liability for 520 NZUs for the emissions year to 31 December 2022 as before.

Based on its emissions return, Hexxus Ltd then submits an annual allocation adjustment showing it is entitled to a further 20 free NZUs (being a final allocation of 320 NZUs) for the 2022 emissions year over the provisional allocation received of 300 NZUs back in May 2022. This means the 2023 income year was an emissions unit shortfall year.

Hexxus Ltd also determines that the provisional allocation for the 2023 emissions year should be 280 NZUs, as its baseline has been reduced with the transition to fully renewable energy.

There are different methods for accounting for the NZU shortfall. Recording the provisional allocation of 300 NZUs together with the 20 shortfall NZUs yields the same outcome as recognising the final allocation of 320 NZUs. In accordance with s ED 1B, this example will use the final allocations of NZUs.

Accrual of the shortfall NZUs

It is helpful to show the shortfall NZUs accrued to the 2023 income year within the final allocation. Since the 20 shortfall NZUs are from the 2022 emissions year, they should be accrued like free NZUs to ensure correct reporting for the 2023 income year. Only shortfall NZUs from April to December 2022 apply to the 2023 income year. Therefore, the shortfall NZUs for the 2023 income year are:

$$\begin{aligned}
 \text{2023 accrual of shortfall NZUs} &= \text{shortfall NZUs} \times 9 \text{ months} \div 12 \text{ months} \\
 &= 20 \times 9 \div 12 \\
 &= 15 \text{ NZUs}
 \end{aligned}$$

As noted, because the shortfall NZUs are included in the final allocation, they are not shown separately in the following calculations.

Accrual of final allocation of NZUs

Like Example | Tauria 3, free NZUs equal to the final unit entitlements for the parts of the 2022 ($320 \times 75\% = 240$) and 2023 ($260 \times 25\% = 65$) emissions years that fall into the income year ended 31 March 2023 must be valued at market value on 31 March 2023 ($240 + 65 = 305 \times \$67.50 = \$20,587.50$) as they are part of the unit entitlement for the income year (s ED 1B(8)(a)). The value of the NZUs on hand is income as closing stock (s CH 1(4)). The same value is then deductible the next year as opening stock (s DB 49(4)).

Figure | Hoahoa 12: Summary of accruals of final allocations of free NZUs

Income year ending	31/03/2022	31/03/2023
9 months from 2021/2022 emissions year	255	240
3 months from 2022/2023 emissions year	80	65
Final NZUs accrual	335	305

This means the summary shown in Figure | Hoahoa 10 is no longer correct. The inclusion of the shortfall NZUs is shown in Figure | Hoahoa 14. Additionally, given that Hexxus Ltd is going to receive the 20 shortfall NZUs in May, Hexxus Ltd intends to immediately surrender these NZUs in discharge of its emissions liability. This means that Hexxus Ltd only needed to purchase 200 NZUs in February 2023.

The new situation under the variation is summarised as follows:

Figure | Hoahoa 13 – Accruals for 2023 income year

Date	Transaction	Emissions year	Income year accrual
31/5/22	Provisional allocation	300	
15/2/23	Purchase of 200 NZUs	200	200
31/3/23	Revaluation of share of 2022 final allocation		240
31/3/23	Revaluation of share of 2023 final allocation		65

Figure | Hoahoa 14 – 2023 income year (including shortfall units)

Date	Description	Cost / market value	No of NZUs	Income	Deduction
May 2022	Provisional allocation of free NZUs	0.00	300	0	0
February 2023	Purchase of NZUs on market	67.00	200		\$13,400.00
March 2023	Deduction for emissions liability – (200 NZUs @ \$67.00 cost plus 310 NZUs @ \$67.50 market value on balance date)			0	\$34,325.00
	Revaluation of free NZUs (including shortfall NZUs) to market value – see Figure Hoahoa 12 (ss ED 1B(8) and CH 1(4))	67.50	305	\$20,587.50	0
	Income under s CH 1(4) for purchased NZUs being revenue account property (RAP)	67.00	200	\$13,400.00	
	Subtotals			\$33,987.50	\$47,725.00
	Net position				(\$13,737.50)

82. The net position of (\$13,737.50) shows in economic terms that Hexxus Ltd is left claiming a deduction for its emissions liability that it incurred based on the cost of the NZUs it needed to purchase plus a further amount. The further amount is the value of 5 NZUs, being the difference between the number of free NZUs to satisfy the emissions liability (310, being 510 less the 200 purchased) and the number of free NZUs from the final allocation accrued to the 2023 income year (305).
83. Having reviewed its 2023 income year to adjust for the unit shortfall, Hexxus Ltd then considers the surrender of these NZUs in May 2023 and the receipt of its next year's initial allocation in Example | Tauria 5.

Example | Tauria 5 – Surrender and receipt of NZUs in May 2023

This example builds on the variation in Example | Tauria 4 that the 2022 income year was a shortfall year and follows the other facts from Example | Tauria 3. This means that this example assumes that Hexxus Ltd knew in February 2023 that it was entitled to a further 20 NZUs and so only purchased 200 NZUs then.

Before considering the surrender of the NZUs, it is useful to review Hexxus Ltd's opening balance of NZUs on hand on 1 April 2023 (for the 2024 income year). Essentially, it is the same 500 NZUs at the same values as the closing balance on 31 March 2023 plus the 20 shortfall NZUs Hexxus Ltd is deemed to hold at 31 March 2023 as shown in Figure | Hoahoa 14.

In May 2023, Hexxus Ltd surrenders its NZUs on hand for the 2022 emissions year and receives its provisional allocation of 280 free NZUs for the 2023 emissions year. Additionally, Hexxus Ltd receives and surrenders the 20 shortfall NZUs from the 2022 emissions year.

After surrendering the NZUs and receiving the next year's entitlement, Hexxus Ltd holds 280 NZUs being the 2023 emissions year's provisional allocation. This is shown in Figure | Hoahoa 15:

Figure | Hoahoa 15 – Hexxus Ltd's NZUs on hand

Date	Hexxus Ltd – NZU account	NZUs	Balance
31 May 2022	Opening balance	0	0
31 May 2022	Provisional allocation	300	300
15 Feb 2023	NZUs purchased	200	500
31 May 2023	Shortfall NZUs	20	520
31 May 2023	Surrendered NZUs	520	0
31 May 2023	Provisional allocation of NZUs	280	280

Value of surrendered NZUs – free NZUs

For the NZUs surrendered in May 2023, the value on surrender is determined under s CB 36.

The free NZUs are valued under s CB 36(3)(b). This treats the surrender value as being the NZU's value under s ED 1(7B). Under s ED 1(7B)(d), NZUs have the value attributed by s ED 1B. Under s ED 1B(8)(a), the NZUs are valued at their market value at balance date. This means the free NZUs are treated as being surrendered in May 2023 at their market value of \$67.50 on 31 March 2023.

Section CB 36(2) confirms that this amount is income for Hexxus Ltd. However, Hexxus Ltd also received a deduction for this amount (as part of the opening value of NZUs at 1 April 2023 being revenue account property under s DB 49(4)). This means the income and deduction cancel each other out. Accordingly, there are no net tax consequences on surrendering the free NZUs for Hexxus Ltd in the 2024 income year.

Value of surrendered NZUs – shortfall NZUs

For the shortfall NZUs in the 2023 income year, these are received in May 2023 and immediately surrendered to help satisfy Hexxus Ltd's liability. Shortfall NZUs are accrued into the relevant income years and are allocated market value on balance date until the shortfall is satisfied. They are then disposed of at this value when surrendered under s CB 36(3)(b).

Section CB 36(2) confirms that the surrender amount is income for Hexxus Ltd. However, as Hexxus Ltd was deemed to hold these NZUs at 31 March 2023, Hexxus Ltd receives a deduction for this amount (as part of the opening value of NZUs at 1 April 2023 being revenue account property under s DB 49(4)). This means the income and deduction cancel each other out. Accordingly, there are no net tax consequences on receiving and surrendering the shortfall NZUs for Hexxus Ltd in the 2024 income year.

Value of surrendered NZUs – purchased NZUs

The purchased NZUs surrendered were acquired in February 2023 for \$67 per NZU.

At 31 March 2023, these NZUs were still valued at \$67 under s ED 1(1). Because the purchased NZUs are revenue account property, s CH 1(4) provides that Hexxus Ltd derived income of the value of the NZUs at 31 March 2023. Effectively, this cancels out the deduction for the cost of the purchased NZUs for Hexxus Ltd in the 2023 income year. However, s DB 49(4) then allows Hexxus Ltd a deduction for this amount in the 2024 income year.

On surrender of those purchased NZUs, s CB 36(2) provides that the amount Hexxus Ltd derives on disposal is income, and under s CB 36(3)(a) the amount Hexxus Ltd is treated as deriving is the cost of the purchased NZUs.

84. The results of Example | Tauria 5 are shown in Figure | Hoahoa 16.

Figure | Hoahoa 16 – Summary of NZU tax treatment 2023 and its impact into 2024

NZUs	2023 income year		2024 income year		Outcome
Emissions liability		31 Mar 23 Deduction of \$34,325.00			Deduction of \$34,325.00
305 free NZUs (including shortfall NZUs)	31 May 22/23 Received for \$0	31 Mar 23 Revalued to market value of \$67.50 → income \$20,587.50	1 Apr 23 Deduction for revenue account property at book value of \$67.50 (\$20,587.50)	31 May 23 Surrender at book value of \$67.50 → income \$20,587.50	Income of \$20,587.50
200 purchased NZUs	1 Feb 23 Purchased for \$67 each → deduction (\$13,400)	31 Mar 23 Income from revenue account property of \$13,400	1 Apr 23 Deduction for revenue account property of (\$13,400)	31 May 23 Surrender at cost of \$67 → income \$13,400	No effect
Net effect					Deduction of \$13,737.50

85. Based on Figure | Hoahoa 16, there are different tax results for the different NZUs.

- The free NZUs give rise to income in the 2023 income year. This reduces the deduction for Hexxus Ltd's emissions liability.
- For the 200 purchased NZUs, the net result for tax purposes is nil. There are corresponding amounts of income and expenditure in each of the 2023 and 2024 income years. However, for Hexxus Ltd, it obtained a deduction for its emissions liability largely based on the cost of the NZUs.

86. The results for the following year (the 2024 income year) are illustrated in Example | Tauria 6.

Example | Tauria 6 – 2024 income year

Hexxus Ltd received the 20 free NZUs that were provided in May 2023 to make up for the shortfall in the 2022 emissions year and then immediately surrendered these. Hexxus Ltd also received the 280 free NZUs that were provisionally allocated in May 2023.

In addition, Hexxus Ltd purchased 200 NZUs for \$65.00 each in February 2024.

In its emissions return filed 31 March 2024, Hexxus Ltd noted that its final allocation for the 2023 emissions year was 260 NZUs.

Hexxus Ltd's emissions liability in NZUs for 2024 income year

As at 31 March 2024, Hexxus Ltd's emissions liability needs to be determined as the 9-month period from 1 April 2023 to 31 December 2023 of the liability for the emissions year ended 31 December 2023 and the estimated liability for the 3-month period from 1 January 2024 to 31 March 2024 (based on production) for the emissions year ended 31 December 2024. The liability to 31 December 2023 is calculated in a return required to be filed by 31 March 2024, being 480 NZUs. Nine months of this is 360 NZUs.

To this amount needs to be added three months of the estimated liability to 31 December 2024. Because it has the production and emission figures for the period 1 January to 31 March 2024 and because of efficiencies it has introduced, Hexxus Ltd estimates its liability for this period as reducing to 400 NZUs.

This means the liability for the first 3 months is 100 NZUs.

Hexxus Ltd has a total liability to 31 March 2024 of 460 NZUs (360 + 100). Having worked out the emissions liability, Hexxus Ltd can now work out its actual deduction.

Hexxus Ltd's deduction for 2024 income year

Hexxus Ltd works out its deduction based on its emissions liability of 460 NZUs. Note that this is Hexxus Ltd's emissions liability for its **2024 income year**, and not the emissions liability of 480 NZUs for the **2023 emissions year** (ending 31 December 2023). As Hexxus Ltd expected to have about 200 NZUs less than it needed (being the 480 estimate less the 280 free NZUs received), it purchased 200 NZUs on the market in February 2024 for \$13,000 (\$65.00 each). This amount is used to determine part of Hexxus Ltd's emissions liability.

The second component is based on the number of NZUs required to be surrendered. From the above calculation, this is 460 NZUs. Of the 460 NZUs, 200 have been valued using the cost of the purchased NZUs. Hexxus Ltd needs a further 260 NZUs to satisfy the surrender liability.

The deduction for these NZUs is based on the market value at 31 March 2024. This is because the market value at balance date is the expected cost of the NZUs required to be surrendered (for which Hexxus Ltd is definitively committed) for the tonnes of carbon emitted.

The market value at 31 March 2024 is \$63. The available deduction is 260 NZUs at \$63 = \$16,380, for a total deduction of \$13,000 + \$16,380 = \$29,380.

This amount is deductible under the general permission for Hexxus Ltd's liability to surrender NZUs.

Accounting for NZUs as revenue account property for 2024 income year

From Figure | Hoahoa 16, the tax accounting opening balance of NZUs on 1 April 2023 was 505 NZUs. This comprised the 305 free NZUs (based on the final allocation entitlements (including the shortfall NZUs) accrued from each of the 2022 and 2023 emissions years), and the 200 purchased NZUs that Hexxus Ltd held at 31 March 2023.

In May 2023, Hexxus Ltd received an allocation adjustment of a further 20 NZUs for the 2022 emissions year (the shortfall NZUs) and the provisional allocation of 280 NZUs for the 2023 emissions year.

As 2024 is an income year that follows a unit shortfall year, s ED 1B(3) is engaged. It requires that the NZUs are valued under subs (4).

Allocated NZUs up to the number of the unit shortfall in the 2023 income year (being the emissions unit shortfall year) are each assigned a value equal to the market value at the end of the emissions unit shortfall year (that is, at 31 March 2023). Any further NZUs allocated are assigned a value of zero. When Hexxus Ltd receives the NZUs in May 2023, 15 of the 20 shortfall NZUs are assigned a value of \$67.50 each as that is the accrual for the period 1 April 2022 to 31 December 2022 treated as a 'unit shortfall' under s ED 1B(9), and the balance of 280 NZUs are each assigned a value of zero as there are no shortfall NZUs for the 2023 emissions year. The remaining 5 shortfall NZUs from the 1 January to 31 March period of the 2022 emissions year would be accounted for in the 2022 income year.

Fifteen of the 20 NZUs received in May 2023 reduce the unit shortfall and unit shortfall value from the 2023 income year to zero under s ED 1B(10)(a) and (b). The 2023 income year then ceases to be a unit shortfall year under s ED 1B(10) – for the purposes of the 2024 income year onwards. Because the unit shortfall of 15 NZUs are valued at market value on 31 March 2023 when they were deemed to be on hand, no income or deduction is triggered on receipt. However, income equal to their tax book value under s CB 36(3)(b) is derived in the 2024 income year when they are surrendered in May 2023 immediately after receipt. As noted at [87], this unit shortfall of 15 NZUs is deemed to be revenue account property and on hand at 31 March 2023. Consequently, an opening deduction is available under s DB 49 in the 2024 income year to offset the income derived when they were surrendered.

The remainder of the NZUs in the 2024 income year are treated as follows:

- The 280 NZUs received in May 2023 as the initial allocation for the 2023 emissions year are valued at \$0 on receipt under s ED 1B(4)(b). Then at balance date on 31 March 2024, 9 months of the 2023 emissions year final allocation for the period 1 April 2023 to 31 December 2023, being $260 \times 75\% = 195$, plus 3 months of the 2024 emissions year final allocation for the period 1 January 2024 to 31 March 2024 being $220 \times 25\% = 55$ (totalling 250 NZUs), are revalued to market value of \$63 at 31 March 2024 under s ED 1B(5) to produce income of \$15,750.
- The cost price of the 200 NZUs purchased in February 2024 for \$65.00 each is deductible under the general permission, but this is offset by a corresponding amount of income that arises under s CH 1(4) at 31 March 2024.
- Therefore, the opening stock of NZUs on 1 April 2024 is $250 @ \$63$ plus $200 @ \$65.00 = 450$ and their value as revenue account property is deductible under s DB 49.

87. A summary of Hexxus Ltd's position in the 2024 income year is set out in Figure | Hoahoa 17.

Figure | Hoahoa 17 – Hexxus Ltd's 2024 position

Date	Description	Cost / market value (\$)	No of NZUs	Income	Deduction
April 2023	Opening stock of free NZUs (including unit shortfall NZUs)	67.50	305	0	\$20,587.50
	Purchased NZUs on hand	67.00	200		\$13,400.00
May 2023	Surrender of free NZUs (including unit shortfall NZUs)	67.50	305	\$20,587.50	
	Surrender of purchased NZUs	67.00	200	\$13,400.00	
	Provisional allocation of free NZUs for 2023 emissions year valued at zero on receipt – s ED 1B(4)(b)	0	280		
February 2024	Purchase of NZUs on market	65.00	200		\$13,000.00
March 2024	Deduction for emissions liability (200 NZUs @ \$65.00 cost plus 260 NZUs @ \$63 market value on balance date)				\$29,380.00
	Revalue the accruals of the final allocations of free NZUs for the 2023 (195) and 2024 (55) emissions years to market value (ss ED 1B(8)(a) and CH 1(4))	63.00	250	\$15,750.00	
	Income under s CH 1(4) for purchased NZUs being revenue account property	65.00	200	\$13,000.00	
	Subtotals			\$62,737.50	\$76,367.50
	Net position				(\$13,630.00)

88. The summary in Figure | Hoahoa 17 shows that when all of the NZUs have been accounted for, Hexxus Ltd's net position is effectively determined as the cost of the purchased NZUs it has on hand at 31 March 2024. The difference is the value of 10 NZUs, being the difference between the number of free NZUs to satisfy the emissions liability (260, being 460 less the 200 purchased) and the number of free NZUs from the final allocation accrued to the 2023 income year (250).
89. Note that Hexxus Ltd still has 20 free NZUs on hand that have not been revalued to market value at balance date under s ED 1B(8)(a) – they remain valued at zero under s ED 1B(8)(b) as they are the amount of free NZUs from the provisional allocation that exceeded the final allocation for the 2023 emissions year of 260 free NZUs. These 20 NZUs are excess NZUs and discussed next.

Excess NZUs

90. Figure | Hoahoa 17 demonstrated what happens when the final allocation is less than the provisional allocation. This results in excess NZUs. A business may receive a provisional allocation of free NZUs that exceeds their final allocation due to falling production or a reduction in the industrial allocation. The allocation adjustment the following May will then result in the participant electing to either offset those excess free NZUs against the provisional allocation for the next income year or return the excess NZUs to an account nominated by the EPA. The "unit entitlement" definition does not include these excess NZUs in the income year when the provisional allocation is received and as a result they are allocated a value of zero at balance date under s ED 1B(8)(b).
91. If the participant elects to have the excess NZUs offset against the following year's provisional allocation, they receive that provisional allocation less the excess NZUs from the prior emissions year.
92. If the participant elects to return the excess NZUs to the EPA this must occur by May following the emissions year end. The resulting transfer will be a disposal under s CB 36, but not a surrender. The free excess NZUs have a value of zero when disposed of and no income is derived from the disposal. The return of excess NZUs is treated as a disposal at zero value under s ED 1B(7)(b).
93. The impact of these provisions is that the participant is taxed based on their final allocation entitlement and the temporary receipt of excess free NZUs is ignored.
94. The above concepts are illustrated in Example | Taurira 7.

Example | Taurira 7 – Excess NZUs for horticulture business

Some horticulture sectors (for example, tomato and cucumber growers using glasshouses) are entitled to free NZUs because of increased ETS input costs like gas heating, even though they do not have emissions liabilities.

Cumbersome Ltd grows cucumbers hydroponically in a heated glasshouse. Cumbersome Ltd receives free NZUs through industrial allocation and its tax balance date is 31 December. Because the tax balance date and emissions years are aligned Cumbersome Ltd does not have to complete any accrual calculations to reflect income derived from its allocation of free NZUs. While Cumbersome Ltd does not create emissions itself, it incurs higher costs because of the ETS, through its extensive gas usage for heating, and receives free NZUs to help subsidise those higher costs.

Cumbersome Ltd's provisional allocation in May 2023 was 300 NZUs, based on the previous year's production levels. However, in mid-2023, a widespread drought caused Cumbersome Ltd's water allocation to be reduced, and Cumbersome Ltd had to reduce cucumber production as a consequence.

Following the reduced production, Cumbersome Ltd's allocation adjustment (based on the final allocation for the 2023 emissions year made in May 2024) was 50 fewer NZUs, that is, 250 NZUs.

Because Cumbersome Ltd received 300 NZUs in the provisional allocation, it received 50 more free NZUs than it was entitled to.

Cumbersome Ltd had the choice under the CCRA of returning the excess NZUs or having them offset against the provisional allocation of NZUs for the 2024 emissions year.

Cumbersome Ltd does not have to determine an emissions liability or acquire NZUs on the market for surrender, because it is not an emitting business. Instead, Cumbersome Ltd can sell the free NZUs it receives on the market and use the funds to offset its higher gas heating costs. The amount derived from any such sale is income.

It may also choose to keep some free NZUs as their price is expected to rise over time.

While 250 of the free NZUs would be valued at market value at balance date on 31 December 2023, the 50 excess free NZUs would not have been included as income at market value at the end of the income year. This is because under s ED 1B(8)(b) they would have been allocated a value equal to zero at year end. Only the actual entitlement to free NZUs (250) is recorded as income at the year-end market value under s ED 1B(8)(a) with any excess assigned a zero value under s ED 1B(8)(b).

Cumbersome Ltd therefore has the option of offsetting the extra NZUs against the next year's provisional allocation or returning them to the EPA and these options and what happens when Cumbersome Ltd decides to keep holding free NZUs for a period spanning several income years are explained next.

Option 1 – Cumbersome Ltd sells the excess NZUs

Instead of holding them through to balance date on 31 December 2023 Cumbersome Ltd sells the free NZUs it received in November 2023 to help offset its increased production costs. The total sale price for the 300 free NZUs is income, and there is no deduction for the cost of the free NZUs as they were valued at zero on receipt.

Having also sold the 50 excess free NZUs, Cumbersome Ltd has no choice but to offset them against its provisional unit entitlement for the 2024 emissions year (which would have then dropped from 300 to 250 free NZUs as it is based on the prior year's actual amount). As a result, Cumbersome Ltd's final allocation entitlement for the 2024 emissions year of 250 free NZUs will be reduced by the 50 free NZUs that have been offset down to 200. This means that while Cumbersome Ltd's final entitlement is still 250 NZUs, it will have only received 200 NZUs. When Cumbersome Ltd is determining its position at its balance date on 31 December 2024, it will need to revalue the 200 NZUs held under s ED 1B(5).

Option 2 – Cumbersome Ltd returns the NZUs

Alternatively, Cumbersome Ltd may decide not to sell the excess free NZUs it receives but to instead return them to the EPA. This means they would not be deducted from the next year's provisional allocation in May 2024. The return of excess NZUs under s 83(6)(b) of the CCRA is not treated as a surrender but is still a disposal for tax purposes under s CB 36(1). The CCRA makes a clear distinction between NZUs that are surrendered for an emissions liability and NZUs that are returned because the provisional allocation exceeds the final allocation.

Returning the NZUs would still be a disposal under s CB 36, but not one resulting in any income under s CB 36(2) because no amount is derived from the disposal. They are required to be transferred to a Crown holding account designated by the EPA by 31 May after the emissions year they relate to under s 83(6)(b)(ii) of the CCRA. The other provisions of s CB 36 do not apply to a return of NZUs that is not a surrender.

Further, the value of those excess NZUs would be zero when allocated to Cumbersome Ltd under s ED 1B(2), as the prior year would not have been an emissions unit shortfall year, and zero again if still held at balance date on 31 December 2024 under s ED 1B(8)(b).

Option 3 – Cumbersome Ltd keeps the final 2023 allocation of free NZUs and sells them in 2025

Under this option Cumbersome Ltd decides to hold on to the final allocation of free NZUs (250) that it received for the 2023 emissions year and returns the over allocation of 50 free NZUs in May 2024. As discussed under Option 1, it must return the market value ($250 \times \$69 = \$17,250$) of its final entitlement that it is holding at balance date on 31 December 2023 as income under s ED 1B(8)(a), with the excess 50 free NZUs being valued at nil.

In the 2024 emissions year, Cumbersome Ltd is entitled to receive a further 250 NZUs as a provisional and final allocation. Additionally, in May 2024, it has to return the over-allocation of 50 NZUs from the 2023 emissions year. Sales of cucumbers are going well so Cumbersome Ltd is still holding all these NZUs at 31 December 2024. Cumbersome Ltd is then holding two different "pools" of NZUs. These are the 250 NZUs each valued at \$69 at 31 December 2023 and the final allocation for the 2024 emissions year of 250 NZUs. For the 2023 NZUs, because they are revenue account property, a deduction is available for the \$69 value in January 2024 under s DB 49(4), with income of the same amount arising at 31 December 2024 under s CB 36(2). The 2024 NZUs need to be revalued to their market value of \$64 each on 31 December 2024 resulting in income of \$16,000 for the 2024 income year.

Because it has renegotiated its gas contract for the next three years at a much higher rate than in the past and the market price for NZUs has been declining in recent months, Cumbersome Ltd decides to sell all free NZUs in August 2025 for \$56.90 each to produce income under s CB 36(2) of \$28,450 for the period ending 31 December 2025. It has a deduction for the opening value of the 2023 and 2024 NZUs of \$33,250 under s DB 49(4) to produce a net tax loss of (\$4,800) for that income year. This is shown in Figure | Hoahoa 18.

Figure | Hoahoa 18: Summary of tax consequences of holding NZUs

Date	Description	Cost / market value (\$)	No of NZUs	Income	Deduction
May 2023	Provisional allocation of free NZUs for 2023 emissions year	0.00	300		
Dec 2023	Revalue final allocation of NZUs on hand (s ED 1B(8)(a))	69.00	250	\$17,250.00	\$17,250.00
Dec 2023	Excess NZUs recorded at nil value (s ED 1B(8)(a))	0.00	50	\$0.00	
Dec 2023	Total income for 2023 income year			\$17,250.00	
Jan 2024	Deduction for revalued NZUs as revenue account property (s DB 49(4))	69.00	250	\$ 0.00	\$17,250.00
May 2024	Return of excess NZUs	0.00	50	\$0.00	
May 2024	Provisional allocation of free NZUs for 2024 emissions year	0.00	250		
Dec 2024	Income for 2023 emissions year NZUs (s CB 36(2))	69.00	250	\$17,250.00	
Dec 2024	Income for 2024 emissions year NZUs (s CB 36(2))	64.00	250	\$16,000.00	
	Subtotals			\$33,250.00	\$17,250.00
Dec 2024	Total income for 2024 income year			\$16,000.00	
Jan 2025	Deduction for revalued 2023 NZUs as revenue account property (s DB 49(4))	69.00	250		\$17,250.00
Jan 2025	Deduction for revalued 2024 NZUs as revenue account property (s DB 49(4))	64.00	250		\$16,000.00
Aug 2025	Sales of all NZUs held	56.90	500	\$28,450.00	
	Subtotals			\$28,450.00	\$33,250.00
	Net position				(\$4,800.00)

Fishing quota emissions units⁶

95. The proceeds from the disposal of "Fishing quota emissions units" issued in 2009 to fishers who held their quota on capital account are treated as excluded income. However, if the quota was held on revenue account, the NZUs allocated to them are on revenue account too and treated in the same manner as free NZUs issued for industrial allocation.
96. This outcome arises from s ED 1(7B)(cb) that provides the value of fishing quota emissions units are:
 - zero at year end when held on capital account and
 - market value at year end when held on revenue account.
97. Those values then flow through to the adjustment provisions for opening and closing stock of NZUs in ss CH 1 and DB 49.
98. This is augmented by ss CB 36(20) and CX 51C(2), which treat a disposal (other than by surrender) of fishing quota emissions units held on capital account as excluded income where the disposal was not by way of surrender for emissions liabilities. In contrast, the disposal of fishing quota units held on revenue account is governed by s CB 36(2) so that if they are sold or surrendered the proceeds will be income.
99. If fishing quota units are surrendered for emissions liabilities they are treated as sold by s CB 36(3) at whatever value they have at that time under s ED 1(7B)(cb).

GST treatment of NZUs

100. NZUs are treated as a supply of services and rather than goods under the Goods and Services Tax Act 1985 (GSTA). Supplies of NZUs are subject to GST, however, most supplies are zero-rated under s 11A(1)(s)–(w) of the GSTA as follows:
 - the transfer of NZUs (other than certain transfers by the Crown that are not relevant in the industrial and removal activities context) (s 11A(1)(s));
 - the surrender of NZUs under s 63 of the CCRA (that is, for emissions) (s 11A(1)(t)); and
 - the supply of services to or by the Crown in consideration for which there is no payment of a price and that is zero rated under paras (s) or (t) above (s 11A(1)(u)); and
 - a disposal of similar types of units to NZUs that are issued by reference to the sequestration or avoidance of emission of human-induced GHGs and verified to an internationally recognised standard (s 11A(1)(w)).
101. Therefore, the transfer or surrender of NZUs is generally zero rated for GST purposes. This means the relevant supplies are technically subject to GST but at a rate of 0%.
102. Where unrelated parties agree that NZUs are to be provided at a future date as part of the consideration for a supply of goods and services, the amount agreed for the NZUs is the value for GST purposes. For example, a producer contracting with a distributor or generator for supplies of natural gas at future dates for an amount of money plus sufficient NZUs to cover the emissions liability on that gas. This is provided for in ss 10(2)(b)(ii) and 10(2B) of the GSTA. For GST purposes the amount agreed can include a nil value for such NZUs.

⁶ See also para [142] of the Appendix

Appendix: Industries in the Emissions Trading Scheme and eligible removal activities

Introduction

103. This Appendix provides more details about:

- the industries in the Emissions Trading Scheme (ETS) (see from [104]);
- removal activities eligible to receive NZUs (see from [132]); and
- fishing quota emissions units (see [135]).

Industries in the ETS

104. Industries or sectors in the ETS are industrial processes, liquid fossil fuels, stationary energy, waste disposal, horticulture, agriculture and synthetic greenhouse gases (SGGs).

Industrial processes

105. Participants in the industrial processes sector are required to record the amount of product they produce annually and submit this in an emissions return. Each product has an emissions factor that estimates the emissions per tonne for that process. The gross tonnage of product is multiplied by this factor to give a total emissions figure. The business is then required to surrender NZUs corresponding to its reported emissions.

106. These obligations apply to:

- iron and steel;
- aluminium (including carbon dioxide (CO₂) and perfluorocarbon emissions);
- clinker or burnt lime (resulting in calcination of limestone or calcium carbonate);
- glass (manufactured using soda-ash); and
- gold (where CO₂-equivalent emissions per year exceed 5,000 tonnes).

Liquid fossil fuels

107. Suppliers of petrol, diesel, aviation gas, jet kerosene, light fuel oil and heavy fuel oil have an obligation to report and surrender NZUs. There are exemptions for international aviation and marine transport, but domestic airlines use fuel covered by the ETS.

108. Principally the obligation applies when the fuel supplier takes fuel from the refinery (now shut and operating as storage for imported product) or imports it. However, large purchasers of liquid fossil fuels can participate voluntarily (that is, opt in) to the ETS.

109. Liquid fossil fuel suppliers do not receive an industrial allocation as they are not considered trade exposed and can pass on their costs to consumers.

110. Generally, coastal shipping and fishing industries do not directly participate in the ETS, but they can face increased costs associated with the ETS. Even though domestic cargo is carried by international parties undertaking coastal shipping, fuel they buy in New Zealand does not incur ETS costs. In contrast, in the fishing industry all fuel from New Zealand includes ETS costs, but fishing fleets in the New Zealand exclusive economic zone can purchase fuel outside New Zealand that may not include such costs.

111. Participants in the liquid fossil fuels sector are required to monitor fuel flows and calculate emissions. This excludes biofuels. Biofuels used in the transport sector are not covered by the ETS.

Stationary energy

112. The stationary energy sector includes all fossil fuels (gas and coal) used in electricity generation and in direct production of industrial heat, as well as geothermal energy. It does not include energy used for transport, emissions from industrial processes, or heating in commercial or residential facilities.

113. The specific activities included are:

- importing or mining more than 2,000 tonnes of coal annually (but not coal exported);
- importing or mining natural gas (but not natural gas that is exported);
- using geothermal fluid to generate electricity or industrial heat where the level of CO₂-equivalent emissions exceeds 4,000 tonnes annually;

- combusting more than 1,500 tonnes of used waste oil to generate electricity or industrial heat;
 - combusting used tyres or waste to generate electricity or industrial heat; and
 - refining petroleum where this involves use of intermediate crude oil.
114. Stationary energy participants required to participate in the ETS are usually upstream such as coal mining. However, companies further down the supply chain can opt to take on a mandatory party's obligation if they purchase more than:
- 250,000 tonnes of coal annually; or
 - 2 petajoules of natural gas annually.
115. An example is an electricity generator that uses coal, so can take on the surrender obligations of the coal mining company it buys from, with the supplier not then being liable.
116. Participants in this sector must report their emissions and surrender NZUs to reflect these. The sector does not receive any industrial allocations because costs can be passed on to consumers.
117. As the ETS applies to emissions generated in New Zealand it does not apply to coal or natural gas exported from New Zealand. The importing country is responsible for those emissions. However, it does apply to emissions from imported coal.

Waste disposal

118. Waste disposal facilities are obliged to report their emissions and surrender NZUs to cover these emissions. This applies to landfill sites but does not apply to clean-fills or sewage treatment facilities. If the facility combusts waste to generate electricity or industrial heat it is not classified as a waste facility.
119. The liability relates to methane emissions and not CO₂, although significant amounts of CO₂ are produced. Reporting involves calculating the gross tonnage of waste entering the landfill annually and multiplying this by an emissions factor. The result then determines the NZUs to be surrendered. Default emission factors from landfills around the country can be used or the facilities can calculate their actual emissions.
120. No industrial allocations are allocated to this sector because landfill operators are not trade exposed and can pass costs on.

Horticulture

121. Growers in the horticulture sector do not have obligations to report their emissions or surrender NZUs but some activities are eligible for industrial allocations based on the type of crop. Eligible activities are the production of fresh tomatoes, fresh cucumbers, fresh capsicums and cut roses.
122. These types of products are grown in greenhouses and face increased heating costs they cannot pass on due to international competition.
123. The industrial allocation for this sector is calculated using production data (weighed tonnage leaving the gate less crate weight) and not actual power costs so it incentivises these producers to switch to sustainable or renewable energy sources, which don't have an ETS cost.

Agriculture

124. Certain agriculture operations are obliged to report their emissions (methane from animals and nitrous oxide from urine, dung and fertiliser) but they are not required to surrender NZUs to account for their emissions.
125. The activities that must be reported are:
- importing, manufacturing or purchasing (other than for on-selling) synthetic fertilisers containing nitrogen above 1 tonne annually;
 - slaughtering ruminant animals, pigs, horses or poultry;
 - dairy processing of milk or colostrum from cows or heifers of at least 500 tonnes of milk solids annually; and
 - exporting more than 20 live cattle, sheep or pigs from New Zealand.
126. Some agricultural activities (the production of whey powder, lactose, protein meal and gelatine) are eligible for an industry allocation on the basis of being EITE.

Synthetic greenhouse gases

127. SGGs included in the ETS are:

- hydrofluorocarbons (HFCs) – gases commonly found in refrigeration and air-conditioning systems, aerosols, fire protection and foam blowing equipment;
- perfluorocarbons (PFCs) – gases most commonly in refrigeration and air-conditioning systems; and
- sulphur hexafluoride (SF₆) – used in gas-insulated switchgear and circuit breaker equipment and in scientific applications.

128. Parties that manufacture or import HFCs or PFCs in bulk, such as in cannisters, are required to report, but not parties importing goods containing these gases. Importers of goods or motor vehicles that contain these elements pay a carbon price through the Synthetic Gas Levy imposed on them. If SF₆ is used in operating electrical equipment (above the 1 tonne threshold), the user is required to register with the ETS.

129. Importers of HFCs and PFCs and users of SF₆ must surrender NZUs to reflect their emissions. Each gas has a global warming potential value set by how much it affects the atmosphere when released and this determines the emissions the importers and users report.

130. Importers or exporters of HFCs have additional responsibilities. Parties to the Montreal Protocol, which include New Zealand, must gradually phase down HFC production and use to prevent depletion of the ozone layer.

131. Exporters of SGGs or those who destroy SGGs are eligible to receive NZUs as this is classed as a removal activity. Similarly, parties that export or destroy HFCs or PFCs may be eligible to receive NZUs provided they are registered in the ETS.

Removal activities eligible to receive NZUs

132. Some industrial processes are recognised as removal activities because they cause a reduction of global warming gases in the atmosphere. Registration is voluntary but it enables the earning of NZUs equivalent to the CO₂ removed (CO₂ – equivalent).

133. Eligible activities are set out in part 2 of sch 4 of the CCRA with minimum thresholds as set out in Figure | Hoahoa 19.

Figure | Hoahoa 19 – Activity thresholds (tonnes of carbon dioxide equivalent)

Activity	Threshold (tonnes of CO ₂ e)
Production of methanol	5,000
Storing carbon dioxide after capture	no threshold
Exporting liquid petroleum gas	300
Exporting bulk HFCs or PFCs	1
Exporting HFCs or PFCs in pre-charged equipment	1
Exporting HFCs or PFCs in motor vehicles	1
Destroying HFCs or PFCs in New Zealand	1

134. Free NZUs issued for removal activities are issued after a return is filed with the EPA for the emissions year detailing the emissions removed. There is no provisional allocation as occurs for industrial allocations.

Fishing quota emissions units

135. Although commercial fishing is not a sector within the ETS, its increase in fuel costs from the ETS was recognised by a one-off free allocation of 700,000 NZUs for holders of fishing quota on 24 September 2009. This allocation was made in September 2010 based on the proportion of quota held at that time.

References | Tohutoro

Legislative references | Tohutoro whakatureture

Climate Change Response Act 2002, ss 4 (“New Zealand unit”), 63, 83, sch 4

Environmental Protection Authority Act 2011

Goods and Services Tax Act 1985, s 11A(1)(s)-(w)

Income Tax Act 2007, ss CB 36, CH 1, CX 51C, DA 1, DB 49, DB 60, subpart ED (“disposals at zero value”, “unit entitlement”), EW 5(3B), YA 1 (“emissions unit shortfall year”, “revenue account property”)

Other references | Tohutoro anō

Environment Protection Agency, Emissions Trading scheme (webpage, 2024)

<https://www.epa.govt.nz/industry-areas/emissions-trading-scheme/>

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Ministry for the Environment, New Zealand Emissions Trading Scheme (webpage, 2024)

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IS 25/25: Income tax – business activity

Issued | Tukuna: 13 November 2025

This interpretation statement gives guidance on whether and when a taxpayer is carrying on a “business” for income tax purposes. This is relevant to whether a person has income from a business under s CB 1 and to other provisions in the Income Tax Act 2007 where carrying on a business is a requirement.

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

REPLACES | WHAKAKAPIA

- Expenditure in establishing a new business within “Setting up or moving a business – what costs may be allowed” *Public Information Bulletin* 64 (October 1971): 6
- Income Tax Act 1976: Confirming that an activity is not a business for income tax purposes, *Tax Information Bulletin* Vol 6, No 4 (October 1994): 16
- Difference between a taxable activity (GST) and a business activity (income tax), *Tax Information Bulletin* Vol 7, No 3 (September 1995): 8
- Income Tax Act 1994: Diminishing business activity request to treat as hobby, *Tax Information Bulletin* Vol 7, No 5 (November 1995): 19

Summary | Whakarāpopoto

1. This statement is about **whether** a taxpayer is carrying on a business for the various purposes of the Act, and **when** a business commences and ceases. This statement is not about whether a business is a specific type of business (eg, a farming, insurance or mineral-mining business), the location of the business, or whether an amount is derived “from” a business.
2. It is important to understand if you are carrying on a business, and when that business is being carried on, because carrying on a business is a requirement of many provisions in the Income Tax Act 2007. In particular, an amount that a person derives from a business is included in a person’s income for tax purposes and the person is allowed a deduction for expenditure incurred in carrying on that business. It is also important to understand that whether there is a business is not necessarily determinative of whether an amount is income or whether a deduction is available. Sometimes amounts will be income or deductible even if there is no business.
3. The term “business” is defined in the Act to include certain things, but the meaning of the term is largely taken from case law.
4. The leading New Zealand case on what constitutes a business is *Grieve*.¹ Deciding whether a taxpayer is in business involves a two-fold inquiry as to the nature of the activities carried on and the intention of the taxpayer in engaging in those activities.
5. As to the first enquiry, the following matters may properly be considered:
 - the nature of the activity;
 - the period over which the activity is engaged in;
 - the scale of operations and volume of transactions;
 - the commitment of time, money and effort;
 - the pattern of activity; and
 - financial results.
6. The second enquiry is the element of intention. A taxpayer’s subjective intention to make a profit, once established is sufficient to satisfy the second enquiry under the *Grieve* business test. However, this subjective intention must be objectively assessed.

¹ *Grieve v CIR* (1984) 6 NZTC 61,682 (CA).

7. A business can be contrasted with other activities, including hobbies, pastimes, non-profit pursuits and even profit-making activities that, for example, lack sufficient scale. "Hobby" is not a defined term. However, it is sometimes used to describe an activity that does not meet the definition of a business because the person carrying on the activity does not have an intention of making a profit or because they have an insufficient level of activity. As a result, case law that discusses the distinction between a business and a hobby involves a standard application of the business test.
8. Passive activities such as holding shares in a subsidiary, share portfolio investment, money lending and property leasing are capable of being a business depending on the particular facts and an application of the *Grieve* business test.
9. In some cases, it may be difficult to distinguish between a person making a payment to other persons who may be in business and a person carrying on business themselves by contracting with others to carry out certain tasks. In these cases, a person is more likely to be carrying on a business themselves if they are involved in oversight, organisation or control of the tasks they are paying other people to carry out.
10. A single transaction does not usually constitute a business, but this factor is not conclusive. Determining whether a single transaction gives rise to a business depends on the facts and an application of the business test.
11. Depending on the facts, a person may carry on multiple businesses or carry on a business while having a full-time job. However, where the person has a full-time occupation or is retired or unemployed, and they devote only a modest amount of time to the other activity, there is a presumption against a business.
12. A company may more readily be found to be in business than an individual. Similarly, it has been stated that any gainful use to which a company puts its assets to make a profit for its shareholders, on its face, amounts to carrying on a business. However, any presumption as to the existence of a business is rebuttable.
13. The correct characterisation of the nature and scope of a business is important to determining whether any income is derived from the business and whether a sufficient nexus exists between any expenditure and the business.
14. The question of when a business has ceased is important as it generally determines the last moment when expenditure can be deducted for tax purposes under s DA 1. A business ceases when the activities cease or are no longer at a sufficient scale to be considered a business, or when there is no longer an intention to make a profit. This usually occurs when a business is winding up but may also occur where a business downscales or ceases temporarily.
15. Although the concept of a taxable activity for GST purposes is similar to a business for income tax purposes, there are important differences. It follows that the fact the Commissioner may accept a taxable activity is being carried on does not mean a business exists.
16. Figure | Hoahoa 1 sets out factors that may be relevant when determining whether a business is being carried on under the business test.

Figure | Hoahoa 1 – Factors that may indicate a “business” is being carried on

This table sets out factors that **may** be relevant when determining whether a business is being carried on under the business test. These are factors only. The factors might not be relevant or determinative on their own or in all cases. Some of these factors will not be relevant for some businesses.

Business	Not a business
The activity has a real prospect of profit. <i>This is not a requirement in itself. It is the genuineness of the intention to profit that is relevant, not whether there is any reasonable prospect of a profit being made.</i> <i>Nevertheless, whether there is a real prospect of profit is a factor, among others, the courts will consider in the objective assessment of a taxpayer's stated intention of making a profit. See [31].</i>	The activity has no real prospect of profit. <i>Again, this is not a requirement in itself. Where there is no real prospect of profit, the courts and the Commissioner may be sceptical of a taxpayer's stated intention to profit.</i>
The activity is commonly carried on as a business.	The activity is typically carried on as a hobby, sport or pastime for recreation or amusement.
The number of transactions is significant.	The number of transactions is low.
The taxpayer's commitment of money, time and effort to the activity is significant.	The taxpayer's commitment of money, time and effort to the activity is low.
The activity is carried on for a sustained period.	The activity is carried on for a short period.
The activity is systematic, repetitive and regular.	The activity is ad hoc or haphazard.
The scale of operations involves significant assets, accepting that not all businesses need significant assets.	No significant assets are involved, accepting that not all businesses need significant assets.
The taxpayer keeps accounts and business records.	The taxpayer does not keep accounts and business records.
The taxpayer seeks professional advice.	The taxpayer does not seek professional advice.
The taxpayer develops a business plan and analyses and monitors transactions.	The taxpayer has no business plan and does not analyse and monitor transactions.
The activity is marketed and advertised, accepting that not all businesses need to market or advertise.	The activity is not marketed or advertised, accepting that not all businesses need to market or advertise

Introduction | Whakataki

17. This interpretation statement gives guidance on whether a taxpayer is carrying on a “business” for the purposes of the Act.
18. The term business is used throughout the Act in many contexts, including the following.
 - Amounts from a business are income under s CB 1 and expenditure is broadly deductible if it is incurred in the course of carrying on a business under s DA 1(1)(b).
 - The presence of a business is required for many of the land taxing provisions in ss CB 6A, CB 6 to CB 15, CB 15B, CB 15C, CB 15D, CB 15E, CB 16A, CB 16 to CB 23, and CB 23B.
 - Income derived from a business may have a source in New Zealand if the business is wholly or partly carried out in New Zealand under s YD 4.
 - The presence or otherwise of a business in New Zealand is relevant to the territorial scope of many regimes (eg, financial arrangements rules, thin capitalisation rules, loss commonality rules, and research and development tax credits).

- For charities, the requirements for the exemption of income differ depending on whether the income is business or non-business income.
 - Many regimes apportion deductions based on business and non-business use (eg, employer-provided accommodation, motor vehicle expenditure, entertainment expenditure, and mixed-use assets).
 - The presence of a business is relevant to the application of the trading stock rules in subpart EB, the depreciation rules in subpart EE, and the ability to claim bad debt deductions under s DB 31.
 - Special provisions and regimes apply to particular types of businesses (eg, farming, forestry, aquaculture, bloodstock, aircraft operators, insurance, life insurance, shipping and mineral mining).
 - The presence of a business can be relevant to the calculation of family scheme income for the purposes of Working for Families tax credits.
19. This statement is about **whether** a taxpayer is carrying on a business for the various purposes of the Act, and **when** a business commences and ceases. This includes the following matters:
- the meaning of “business” (see from [21]);
 - the difference between a business and other activities (see from [48]);
 - whether passive activities can be a business (see from [57]);
 - a person’s involvement in a business (see from [80]);
 - whether a single transaction can give rise to a business (see from [86]);
 - whether a person can carry on multiple businesses (see from [92]);
 - the scope of a business (see from [102]);
 - when a business commences (see from [117]);
 - when a business has ceased or been suspended (see from [130]);
 - the difference between a business and a taxable activity (see from [160]); and
 - that the existence of a business will not necessarily be determinative of whether an amount is income or whether a deduction is available (see from [166]).
20. This statement is not about whether a business is a specific type of business (eg, a farming, insurance or mineral-mining business), the location of the business, or whether an amount is derived “from” a business.

Analysis | Tātari

Meaning of “business”

21. Guidance aimed at a more general audience (including some Inland Revenue website guidance) uses the term “business” in a general sense to refer to a taxpayer who is carrying on an activity that may be taxed. The general usage of the term business may not always align with the legal test described below.
22. “Business” is defined broadly in s YA 1 as including “any profession, trade, or undertaking carried on for profit”.

YA 1 Definitions

In this Act, unless the context requires otherwise,—

...

business—

- (a) includes any profession, trade, or undertaking carried on for profit:
- (b) includes the activities of—
 - (i) a statutory producer board:
 - (ii) an airport operator:
- (c) is further defined in section DD 11 (Some definitions) for the purposes of subpart DD (Entertainment expenditure)

23. The definition of business includes certain things but largely the term “business” has the meaning given to it by case law.

24. The leading New Zealand case on what constitutes a business is *Grieve*.² In the leading judgment, Richardson J confirmed that the statutory definition does not add anything to the common meaning of the word and does not catch anything that would not otherwise be caught.³
25. On the meaning of “business”, Richardson J said:⁴
- ... Underlying each of the words in the definition in sec 2 and the term “business” itself when used in the context of a taxation statute is **the fundamental notion of the exercise of an activity in an organised and coherent way and one which is directed to an end result**. And the definition itself proceeds to identify its concern that the enterprise be one carried on “for pecuniary profit”. [Emphasis added]
26. Richardson J went on to state that deciding whether a taxpayer is in business involves a two-fold inquiry as to the:⁵
- nature of the activities carried on; and
 - intention of the taxpayer in engaging in those activities.

Nature of the activities carried on

27. As to the first enquiry – the nature of the activities carried on – Richardson J said the following matters may properly be considered:⁶
- the nature of the activity;
 - the period over which the activity is engaged in;
 - the scale of operations and volume of transactions;
 - the commitment of time, money and effort;
 - the pattern of activity; and
 - financial results.
28. Richardson J added:⁷
- It may be helpful to consider whether the operations involved are the same kind and are carried on in the same way as those that are characteristic of ordinary trade in the line of business in which the venture was conducted. **However, in the end it is the character and circumstances of the particular venture which are crucial.** Businesses do not cease to be businesses because they are carried on idiosyncratically or inefficiently or unprofitably, or because the taxpayer derives personal satisfaction from the venture. [Emphasis added]
29. In *Stockwell*,⁸ McKay J observed that the presence or absence of the above factors does not conclude the matter, but rather they are relevant considerations that involve questions of degree.

Taxpayer’s intention

30. The second enquiry is the element of intention. It is the taxpayer’s subjective intention to make a profit that is relevant, although this must be objectively assessed.
31. In *Grieve*, Richardson J said that a taxpayer’s statements about their intentions are relevant in this respect, but actions often speak louder than words.⁹
32. Similarly, Richardson J observed that courts are justified in viewing circumspectly a claim that a taxpayer genuinely intended to carry on a business for profit when looked at realistically there seems no real prospect of profit.¹⁰ However, he went on to state that an actual intention, once established, is sufficient and that it is the genuineness of the intention to profit that is relevant, not whether there is any reasonable prospect of a profit being made.

² *Grieve v CIR* (1984) 6 NZTC 61,682 (CA). See also Richardson J’s summary of his findings in *Grieve* in *Calkin v CIR* (1984) 6 NZTC 61,781 (CA).

³ At 61,687.

⁴ At 61,688.

⁵ At 61,691.

⁶ At 61,691.

⁷ At 61,691.

⁸ *CIR v Stockwell* (1992) 14 NZTC 9,190 (CA) at 9,196.

⁹ At 61,691.

¹⁰ At 61,691.

33. Richardson J also stated:¹¹

It may be proper, too, to approach with some scepticism asserted intentions which on any objective appraisal of external factors seem incapable of realisation. But, unless required by the statutory language, that testing process cannot be elevated into an independent ingredient to be established before the activity is recognised as a business.

34. In *Lawrence*, Fisher J put it this way:¹²

It is plain that in asking whether the taxpayer's purpose in pursuing the undertaking was "for pecuniary profit" one must apply a subjective test. The test is not to determine whether on an objective appraisal the undertaking would ever have been financially viable, still less to rely upon the actual history of the undertaking with the benefit of hindsight and the knowledge that the undertaking did not in fact result in any pecuniary profit. The requirement is to place oneself in the position of the taxpayer at the time that the undertaking was pursued and to ask what his or her actual purpose was at that time.

35. In *Mainzeal Holdings Ltd*, the Court of Appeal stated:¹³

A taxpayer claiming a deduction under s 104(b) does not have to show that, realistically, there was a reasonable prospect of profit. The existence of a genuine intention, however ill-founded, to carry on business for profit is enough. But a claimed intention may be viewed with some scepticism if, on an objective examination of the realities at the time it appears that, even in the longer term, a profitable outcome was impossible or highly unlikely. Lack of a reasonable prospect of profit may indicate that, no matter what legal entitlement to a profit may have existed, the taxpayer did not make the expenditure with that intention.

36. Having a real prospect of making a profit is not a separate requirement for having a business. However, it is a factor that the courts will consider in determining the genuineness of a taxpayer's stated intention of making a profit.
37. *Mainzeal* is an example of a case where the prospect of profit was considered, not as a separate requirement, but among other factors, in evaluating whether a taxpayer had an intention of profit. In *Mainzeal*, the taxpayer claimed deductions under (what is now) s DA 1(1)(b) for payments the taxpayer made under a joint venture agreement with its Australian subsidiary for the purpose of exiting from two failed property developments. The Commissioner argued the deductions were not allowed because the taxpayer did not have an intention of making a profit, so was not carrying on a business as required by the section. The Court of Appeal noted that the taxpayer bore the burden of proof but did not put before the Court evidence about how a profit would be properly calculated under the joint venture. The Court of Appeal also noted the High Court's finding about evidence given by witnesses for the taxpayer. The High Court had found the evidence, about the reasons for and the nature of the relevant payments, unclear and unconvincing. The Court of Appeal stated that a claimed intention of profit may be viewed with some scepticism if on an objective examination of the realities it appears that, even in the longer term, a profitable outcome was impossible or highly unlikely. The Court of Appeal discussed, over several paragraphs, the prospect of profit for the joint venture. The court concluded that there was plainly no prospect of profit for the joint venture and the taxpayer did not establish that it genuinely had a profit-making intention.
38. In some cases, the way that a taxpayer is set up may provide clear support for a stated intention of making a profit. For example, if a company is set up to carry on an income earning activity, has a detailed business plan and has equity investment from investors who expect a return on their investment, the company is likely to have an intention to make a profit.
39. Some activities are expected to make losses for several years before they make a profit. Persons carrying out these activities may have detailed business plans with projections of when they expect to make a profit. They may also have external funding support to cover their expenses in the first years of operation. The fact that persons carrying out these activities expect to make losses initially does not preclude them from having an intention to make a profit.
40. The fact that a person has not made a profit in past years does not mean that they do not intend to make a profit in the future. However, in some cases, past performance may be a relevant factor to consider (among other factors) in determining whether a person has an intention to make a profit. It may be relevant to ask what has changed since the earlier years where losses were made.
41. Some activities may have a high risk of failure. This does not preclude persons carrying on these activities from having an intention to make a profit. Again, it is the genuineness of the intention to profit (objectively assessed) that is relevant.
42. In some cases, if a person has another purpose for carrying on an activity, it may be harder to establish an intention of making a profit. This may be the case with some hobbies, pastimes, and non-profit pursuits (see [48]).

¹¹ At 61,689.

¹² *Lawrence v CIR* (1994) 16 NZTC 11,263 (HC) at 11,266.

¹³ *Mainzeal Holdings Ltd v CIR* (2001) 20 NZTC 17,409 (CA) at [25].

43. In summary:

- The taxpayer has the burden of proving, to the balance of probabilities, that they have an intention to make a profit.
- It is the taxpayer's subjective intention to make a profit that is relevant.
- It is the genuineness of the intention to profit that is relevant, not whether there is any reasonable prospect of a profit being made. An actual intention, once established, is sufficient.
- A taxpayer's statements about their intentions are relevant, but the taxpayer's intention must be objectively assessed.
- If there is no real prospect of profit, the courts (and the Commissioner) are justified in being sceptical of a taxpayer's claim that they intend to make a profit.
- A real prospect of making a profit is not an independent requirement, but it is a factor, among others, that a court will consider in evaluating whether a taxpayer has an intention of making a profit.

The test is one of intention, not motive

44. The test is one of intention, not motive.¹⁴ For example, a charity can have an intention of making a profit, even if their motive is to fund their charitable activities.

Meaning of profit

45. In *Grieve*, Richardson J considered the meaning of "profit" for the purposes of the definition of business. He said:¹⁵

It may readily be assumed ... that Parliament intended that the profit of which the definition speaks is one that is to be ascertained on ordinary commercial principles affecting the type of undertaking in question.

46. Richardson J further elaborated that profit cannot sensibly be equated with profit for tax purposes and that whether special tax deductions and incentives should be taken into account in assessing profitability depends on the context:¹⁶

... I am inclined to think that what is required is to assess the overall financial result that is intended in order to determine whether or not in one form or another a pecuniary profit is being sought. No doubt there will be other problems that arise for consideration in determining what items are to be taken into account and what are to be excluded from account in arriving at that pecuniary profit. They can best be considered in their own context rather than in a vacuum.

47. An intention to make a profit could in some cases be established, at least in part, from an intention to make a capital gain or from an intention to receive tax credits. In *Case 2/2012*, the TRA held that a taxpayer had an intention to make a profit from a rental property activity. This was because the taxpayer had an intention to make capital gains from the rental properties (in the long term) and an intention to receive working for families tax credits (for the periods in dispute, the taxpayer's rental losses reduced the taxpayer's family scheme income and increased the taxpayer's entitlement – this is no longer possible after a law change).¹⁷

The difference between a business and other activities

48. A business can be contrasted with other activities, including hobbies, pastimes, non-profit pursuits and even profit-making activities that, for example, lack sufficient scale. In *Grieve*, Richardson J said that the definition of "business" allows the Commissioner and taxpayers to consider whether an activity has been transformed into a business.¹⁸

49. In *Case K37*, Judge Barber said:¹⁹

An undertaking carried on for profit in the present context is to be distinguished from a hobby, pastime, game, recreation, sport, or a "flutter", of a less consuming, organised and involved activity.

50. "Hobby" is not a defined term. However, in case law it is sometimes used to describe an activity that does not meet the definition of a business because the person carrying on the activity does not have an intention of making a profit or has an insufficient level of activity. As a result, case law that discusses the distinction between a business and a hobby involves a standard application of the business test.

¹⁴ *Grieve* at 61,688.

¹⁵ At 61,691.

¹⁶ At 61,692.

¹⁷ *Case 2/2012* (2012) 25 NZTC 1,014. For a critique of *Case 2/2012* see Lindsay Ng, A taxing decision for rentals, Journal – New Zealand Institute of Chartered Accountants, 5 October 2012: 30.

¹⁸ At 61,689.

¹⁹ *Case K37* (1988) 10 NZTC 314 (TRA) at 320.

51. The fact a person might be indulging in their interests and enjoying their activity does not prevent the activity from being a business. In *Edgecombe*,²⁰ the taxpayer argued that his activity, which involved racing and breeding horses, was merely a hobby. However, based on the facts, the High Court concluded that the taxpayer had been carrying on a business. The court held:²¹

... there can be little doubt that the conduct and the activities undertaken by the appellant showed a scale and volume of transactions and necessarily involved a commitment of time and money which are very similar in character to the carrying on of an ordinary business. **That the appellant was indulging his interest and enjoying his activity is not to be doubted but I think that in the end it was not just as a hobby but with an intention to make a pecuniary profit.** [Emphasis added]

52. *Case F55*²² concerned a husband and wife who carried on a garage business in partnership and also derived earnings from stockcar racing. The taxpayers argued the stockcar racing activity was a hobby. Judge Barber agreed it was a hobby. He said:²³

I find as a fact that Mr H was merely pursuing a hobby on the basis that he hoped that year by year he would average out winnings to about equate expenses. **I find that the activity was not with a view to profit but with a view to fun and prestige. There might have been a reasonable prospect of making a profit but not in a business or commercial or money making sense - only in a sporting sense.** Winnings depended not just on skill but on luck and for some reason or other Mr H seemed to have a large share of luck. [Emphasis added]

53. *Case F55* also illustrates that even if there is a significant amount of assets, money spent and time devoted to an activity, it will not be a business if the intention of making a profit is missing.
54. Many other cases have considered whether an activity carried on by a taxpayer is a business or hobby or is carried on for private purposes. The contexts include horse breeding, hunting, art, boat chartering, farming, gambling and vintage car restoration.
55. For further discussion of this topic in the context of content creators, see **IS 21/08: Content creators - tax issues**.²⁴
56. The difference between a business and other activities is illustrated in Example | Tauira 1 and Example | Tauira 2.

Example | Tauira 1 - Raising cattle on a small rural property

Zaid recently purchased a 4-hectare rural property outside of Hamilton in which to live.

He raises five beef cattle on the land to keep the grass down, fill the freezer and to sell to cover expenses.

Zaid regularly moves the cattle between paddocks and maintains water supply and fences when required. He is able to do this in his spare time and also has a full-time job in the city.

Zaid needs to buy feed for the cattle and pays for vet bills and other expenditure related to the cattle. Overall, if Zaid were to calculate all his expenditure related to raising the cattle, he would likely find that he is making a loss from this activity.

Zaid is considering selling the land, but the sale would be subject to the bright-line test if the land was "residential land". Zaid wants to know if his cattle raising would be considered a farming business (if it is, the land will be "farmland" and, therefore, not "residential land", and the bright-line test would not apply).

Zaid's cattle-raising activity does not constitute a business.

Applying the first stage of the two-fold inquiry in *Grieve*, the scale of operations is very low – he only has a 4 acre property and 5 cattle; the volume of transactions is very low – he will be selling only some of the 5 cattle he keeps; the commitment of time, money and effort are relatively low – he looks after the cattle in his spare time while also working in a full time job; and the financial results are very low – the money he receives would not even cover his expenses. Therefore, the nature of his activity does not support the existence of a business. It is not necessary to go on to consider the second stage involving intention to make a profit.

Therefore, the bright-line test may apply to the sale of the land.²⁵

²⁰ *Edgecombe v CIR* (1991) 13 NZTC 8,140 (HC).

²¹ At 8,146.

²² *Case F55* (1983) 6 NZTC 59,840 (TRA).

²³ At 59,848.

²⁴ IS 21/08: Content creators - tax issues *Tax Information Bulletin* Vol 33, No 10 (November 2021).

²⁵ See QB 25/13: When is the sale of a lifestyle block excluded from the bright-line test?

Example | Taura 2 – Sportsperson²⁶

Nani is a keen athlete who has represented New Zealand in her favoured event of hammer throwing for more than 5 years. She does this in addition to having full-time employment when she is not away competing.

Nani regularly competes in high-level competitions in New Zealand and overseas. Over the last few years, she has regularly placed in the top 20 world rankings and has received some prize money, although the amounts involved are not large. She receives a regular training grant from a high-performance sports academy and received a one-off payment for winning a bronze medal at a recent international competition.

Nani also earns money from a sponsorship deal and from her social media accounts.

However, the costs involved in competing in these events, including travel expenditure for her and her coach are considerable. When these costs are considered, despite the multiple income streams, Nani has never come close to making a profit from competing and she has relied on the income from her job to fund some of her costs.

To make a profit, her manager estimates she would need to consistently place top five in the hammer-throw world rankings and secure a more lucrative sponsorship deal. Placing in the top five is absolutely one of Nani's goals, but realistically she is aware that her chances of achieving this are low. Nani's recent training and results relative to her competitors do not suggest that she is likely to place higher in the rankings this year. Nevertheless, Nani states that she does have an intention of reaching her goals and, therefore, making a profit.

Nani wants to know whether the amounts she derives are taxable under s CB 1 and whether she can claim deductions for her expenses.

The nature of the activity, hammer-throw, is not indicative of a business. Although the ability for a person to sustain a career as a professional athlete has increased in recent years, it is very difficult to make a living from competing in the hammer-throw event. The fact that Nani still maintains a full-time job, and that she relies on her salary to fund some of the costs of competing, suggests that the competition activity is not a business. Further, although Nani is pursuing multiple income streams, overall, the financial return is not substantial and is somewhat erratic (in terms of prize money). On the other hand, the commitment of time, effort and money in her spare time is significant.

Although Nani states she has an intention of making a profit, this must be tested against the objective evidence. It is very difficult to make a living from competing in the hammer-throw event. Over the last five years Nani has never come close to making a profit and there is no suggestion from her recent training and results relative to her competitors that she will be more competitive this year. Realistically, there appears to be little prospect of making a profit. It appears that Nani competes for the personal satisfaction and enjoyment, not to make a profit.

Taking into account the *Grieve* factors, in particular the nature of the activity and the financial results, it will be difficult for Nani to show that she is in business and is able to claim deductions.

This means that even if Nani has an especially good year in which she does manage to make a profit, this will not be taxable (the answer could change if this is not a one-off occurrence). It also means that Nani cannot claim deductions or offset losses from her activity against her other income.

Whether passive activities can be a business

57. A question that arises is whether a passive activity can be a business. This question often arises in the context of holding companies, share portfolio investment, money lending and property leasing.

26 Comparisons might be drawn between Example | Taura 2 and the Australian case of *FCT v Stone* 2005 ATC 4234 (HCA). In *Stone*, a javelin thrower, in a similar (but slightly different) situation to Nani in Example | Taura 2, was found to be carrying on a business and, therefore, various receipts were included in her income.

Although Example | Taura 2 is inspired by the facts in *Stone*, the facts in Example | Taura 2 have been deliberately designed so as to raise doubt about whether Nani intended to make a profit. This design included making Nani less successful than the taxpayer in *Stone*.

Also, Australian income tax law is different from New Zealand law. The Australian legislation, the Income Tax Assessment Act 1997 (Australia), does not have an equivalent to s CB 1. Instead, an amount that is derived from a business is included in income under s 6-5 of the Income Tax Assessment Act 1997 (Australia), which includes income according to ordinary concepts.

Also, in New Zealand, an intention to make a profit is required to have a business. In Australia, an intention to make a profit is treated as a factor to be considered – see *Stone* at [55]. A comparison with *Stone* in particular is made more difficult because little was said in the case about whether the taxpayer had an intention to make a profit or the level of the taxpayer's expenditure.

58. The question is particularly relevant to charities. A charity's business income can be exempt under s CW 42 only to the extent its charitable purposes are carried out in New Zealand.²⁷ In contrast, the exemption for non-business income under s CW 41 is not subject to a territorial restriction.
59. For further discussion of the business test in the context of charities, see **IS 24/08: Charities – business income exemption**.²⁸

Holding companies

60. Corporate groups are often organised under a holding company. The question is sometimes asked whether a holding company is in business. This may be of limited relevance if a consolidated group is used.
61. It will be relatively common for holding companies to carry on business.²⁹ However, whether a holding company is in business depends on the facts in each situation and applying the *Grieve* business test.
62. If a holding company does no more than benefit from holding shares in a subsidiary, then it may not satisfy the first stage of the *Grieve* business test. However, if, for example, a holding company provides corporate services to its subsidiaries in return for fees, it may satisfy the first stage of the test.
63. With respect to the second part of the *Grieve* business test, a holding company will usually have an intention to make a profit because it will usually intend to derive dividends or benefit from an increase in the value of the shares held in the subsidiaries. In considering whether a holding company has an intention of making a profit, profit is to be ascertained on ordinary commercial principles affecting the type of undertaking in question (as noted in *Grieve* and discussed from [45]). An intention to profit from receiving dividends from its subsidiaries or from an increase in the value of shares held in subsidiaries could satisfy the intention to profit requirement.
64. This is illustrated in Example | Tauria 3.

Example | Tauria 3 – Holding company

The Property Group Limited is the holding company of a group of companies that specialises in property development. Each development is undertaken in a separate special purpose subsidiary that the holding company wholly owns. The holding company receives dividends from subsidiary companies as property developments are completed.

All staff in the group are employed by the holding company, which is responsible for identifying property development opportunities, negotiating the acquisition of land for that purpose and obtaining finance, as well as providing operational and administrative support for the subsidiaries.

All expenditure of a revenue nature the holding company incurs is on-charged to its subsidiaries by way of intra-group management fees on a full cost recovery basis such that the holding company generally breaks even each year. In the current income year, the company's financial accounts show management fees totalling \$110,000 and a small operating surplus of \$1,100 (due to a timing issue with the on charging of some of the fees). The company wishes to claim a deduction under s DA 1 for its expenditure.

Applying the first stage of the *Grieve* test, the holding company has a sufficient level of activity to give rise to a business. The only question is whether the company has an intention of making a profit.

The level of intra-group management fees on-charged to its subsidiaries means the holding company will generally not make operating surpluses. The holding company will generally break even or have relatively small surpluses or losses. This is a factor that could point to the company not having an intention of making a profit, and so not being a business for the purposes of s DA 1(1)(b).

However, as noted in *Grieve*, "profit" is to be ascertained on ordinary commercial principles affecting the type of undertaking in question. Here, the holding company has an intention to make a profit in a relevant sense – from dividends that are paid to it on the completion of property development projects.

Therefore, the holding company is carrying on a business.

27 Section CW 42(3) contains an extended definition of "business" for this purpose.

28 IS 24/08: Charities – business income exemption *Tax Information Bulletin* Vol 36, No 10 (November 2024): 3 at [24]–[35].

29 *Rangitira Ltd v CIR* (1996) 17 NZTC 12,727 at 12,730. See also from [98].

Share investment

65. The issue in the context of share investment is generally whether gains on share disposals are taxable under either s CB 1 (amounts derived from business) or s CB 5 (business of dealing in personal property), or whether losses on share disposals are deductible under s DA 1(1)(b). Even if there is no business of dealing in shares, amounts derived from share disposals may be income under other provisions of subpart CB, for example, under s CB 3. Income derived from share investment is discussed in **IS 24/10: Income tax – Share investments**.³⁰
66. Whether share investment constitutes a business is illustrated in Example | Tauria 4.

Example | Tauria 4 – Online investment

Hone started using an online investment platform in November 2020. Over the next few months, he enjoyed making trades and started investing more time and money into buying shares.

Hone was employed for 30 hours a week and spent his free time making trades. Hone invested around \$20,000 in the share market and used the profits from sales to supplement his living costs and re-invest in more shares.

Hone typically didn't hold shares for more than a few months, unless he thought they would peak in value later. He didn't plan to hold any shares long term and didn't consider dividends when purchasing shares.

Hone has an intention to profit from share sales, but his level of activity and amount of time and money spent on the share market do not indicate he is in a business of share dealing. His level of activity does not indicate he has an organised plan that amounts to a profit-making undertaking or scheme.

While Hone may not be in a business of share dealing, the amounts he receives from his share sales are still taxable (and losses are deductible) because the facts indicate that he acquired shares for the dominant purpose of disposal.

Money lending

67. In the context of money lending, the issue is typically whether a taxpayer has a "business of dealing in or holding financial arrangements" so that a bad debt deduction can be claimed under s DB 31.
68. In *Case Z21*,³¹ the taxpayer, a trust, claimed a bad debt deduction on the basis it was in the business of holding financial arrangements under (what is now) s DB 31. The taxpayer had made three high-risk loans over two years. Judge Barber rejected the Commissioner's argument that the activity of money lending, of itself, gave rise to a presumption that there was not a business because it was passive. Instead, Judge Barber confirmed it was necessary to apply the *Grieve* factors. He said:³²

There is no dispute that the taxpayer trust intended to profit from its activity of holding the DW Ltd loan, the L loan and the first and second restructured N 2000 Ltd loans. Therefore, the only issue is whether, having regard to the factors in *Grieve* and other relevant case law, the disputants' activity was carried on in an organised and coherent manner and with sufficient continuity and extent to be the activity of carrying on a business of holding financial arrangements.

69. On the facts, Judge Barber concluded there was "just, and only just, a sufficient level of activity to support the trustees' intention of profit so as to constitute a business of money lending".³³ In coming to this conclusion, Judge Barber considered the factors set out in *Grieve* and made the following comments.
- The taxpayer's period of activity was for two years. Judge Barber described the period of activity as a very relevant factor but also noted that many businesses only operate for such short periods.
 - In terms of the scale of operations, Judge Barber appears to have regarded the taxpayer's scale of operations as consistent with a small business.
 - The volume of transactions was low.
 - Judge Barber described the taxpayer's pattern of activity as the making of somewhat risky loans to seek a high return.
 - Judge Barber appears to have accepted that the commitment of money was limited but nevertheless was consistent with a business that was making a start.

30 IS 24/10: Income tax – share investments *Tax Information Bulletin* Vol 37, No 1 (February 2025): 13.

31 *Case Z21* (2010) 24 NZTC 14,286 (TRA).

32 At 14,297.

33 At 14,300.

- Judge Barber agreed with the taxpayer's argument that the commitment of time and effort was substantial in respect of due diligence and recovery actions undertaken. Judge Barber found that much consideration went into each transaction and that much effort was put into the recovery of loans made.
 - The financial results were poor.
70. In *Case M118*,³⁴ the taxpayer claimed a bad debt deduction for a loan she had made to her son under (what is now) s DA 1. One of the issues the Taxation Review Authority considered was whether the taxpayer was in the business of money lending. In addition to the loan to her son, the taxpayer had made three retail investments and lent money to a company owned by another son. Judge Barber said:³⁵
- I find that a simple application of the criteria set out in *Grieve and Anor v C of IR* (1984) 6 NZTC 61,682; (1983) 6 TRNZ 461 shows that although the nature of the activity carried on by the mother could be consistent with that of a business, it is doubtful whether she ever intended to be in business³⁶ and when, as suggested by Richardson J at NZTC p 61,691; TRNZ p 471, consideration is given to the scale of operations, the volume of transactions, the commitment of time, money and effort, and the pattern of activity, I could not find a business to exist.
71. In summary, the question of whether a taxpayer has a business of dealing in or holding financial arrangements depends on a straightforward application of the *Grieve* factors. This is illustrated in Example | Tauira 5.

Example | Tauira 5 – Family trust investment

The Alexandra Trust is a family trust that holds various investments, including property, shares, bonds and term deposits. The trust has also made a loan of \$200,000 to a beneficiary at a market rate of interest. The bonds and term deposits have a combined value of about \$800,000 in six parcels that are typically held to maturity for a three to five-year term and rolled over. Due to the nature of the investments, the trust does not spend a substantial amount of time on due diligence or on the recovery of amounts invested.

A company in which the trust has \$150,000 of bonds defaults on the bonds, and the trust seeks to claim a bad debt deduction under s DB 31. The issue is whether the trust is in the business of holding or dealing in financial arrangements for the purposes of that section.

The bonds, term deposits and loan to the beneficiary are financial arrangements. The holding of financial arrangements may constitute a business. The trust holds its investments for the purpose of making a profit by receiving interest payments. The trust has held its investments for an extended period. The scale is significant in absolute terms (\$1 million), but very low when compared with the scale of financial institutions that carry on a business of holding or dealing in financial arrangements. The trustees' commitment of time and effort is low, as the investments are generally reviewed only annually and on maturity. The pattern of activity is regular but low. The financial results are in line with low- to medium-risk long-term investments.

It is considered that the trust is not carrying on a business of holding or dealing in financial arrangements. Although the trust has an intention of making a profit, applying the first stage of the *Grieve* test, the scale of operations, volume of transactions and commitment of time and effort are insufficient to give rise to a business.

This is a different conclusion from that reached on the facts in *Case Z21*. The key difference between this example and *Case Z21* is that, in *Case Z21*, the TRA found the taxpayer's commitment of time and effort to be substantial in respect of due diligence and recovery actions undertaken in that case. The same is not true in this example.

Property leasing

72. Rent and other revenues that an owner of land derives from leasing land is specifically included in the person's income under s CC 1 (and deductions may be available for expenses incurred in deriving this income) without the need to establish the existence of a business. However, sometimes it will be relevant to consider whether a property leasing activity is a business.

³⁴ *Case M118* (1990) 12 NZTC 2,755 (TRA).

³⁵ At 2,758.

³⁶ With regard to Judge Barber's comment that "it is doubtful whether she ever intended to be in business" it should be remembered that the relevant question, established in *Grieve*, is whether the taxpayer intended to make a profit.

73. Whether the activity of property leasing is a business depends on an application of the business test set out in *Grieve*. Where a taxpayer leases multiple properties or derives significant rental income, it is likely the activity will constitute a business. Where a taxpayer leases a single property, it is possible the activity may constitute a business, but this will depend on the facts.
74. The following discusses some cases where the courts have considered whether property leasing can be a business.
75. In *Dick*,³⁷ the Court of Appeal considered whether passive rental income derived by a charitable trust was exempt income under (what is now) s CW 42. The trust originally earned income from gaming machines, but to preserve an income stream it acquired several properties from which it derived rent. The leases were long-term net rent leases under which the tenants were responsible for maintenance. The taxpayer argued that the investment in the properties was passive, so not a business. Salmon J quoted the *Grieve* business test and concluded:³⁸
- In our view there is no doubt that the property related transactions constitute a business. Substantial incomes were received from the properties. There is evidence of a profit making intention.
76. Similar conclusions have also been reached by the courts in other contexts. In *Case G44*,³⁹ the taxpayer, an individual, owned two residential properties. He lived in one property, in which he rented the spare rooms, and rented the other property in its entirety. The taxpayer sought to offset losses from the rental activity against his other income on the basis he was in business.⁴⁰ Sheppard DJ applied the *Grieve* business test and concluded:⁴¹
- Considering first the nature of the activities carried on, letting of residential accommodation has a character which can be consistent with business. The objector had been engaged in those activities for several years, certainly since before 1978, and had continued them. The scale of operations had increased with the addition of the house at S (and subsequently increased further with the acquisition at P). The commitment of time and effort was not equivalent to full time employment, but the commitment of money was considerable for a single proprietor. It is in the financial results that the circumstances are not so consistent. Yet I bear in mind that businesses are not necessarily profitable in any year or even group of years, particularly as they are being built up. Looking at the first part of the inquiry overall, I conclude that the facts are consistent with the objector carrying on a business.
- Concerning the objector's intention, his own evidence was unequivocal and unshaken. He intended to make a profit from his activities, though not at the expense of the longer term capital growth and investment aspects of the undertaking. Although he had not produced successful results (except in 1980 in respect of the property at S) I find that he was carrying on the activities in respect of both properties with the intention, which was not entirely unrealistic, of making a pecuniary profit.
77. In contrast, in *Case L102*,⁴² Judge Barber held that a taxpayer who let four rooms in his home to flatmates was not in business as there was not significant enough scale of operations or volume of transactions and observed that he thought it would be rare for an isolated renting transaction to constitute a business.
78. In *LD Nathan*,⁴³ the High Court considered whether the taxpayer, the property holding company for a retail group, was entitled to a deduction for expenditure incurred insulating a building under (now repealed) s 125 of the Income Tax Act 1976. This section allowed a deduction for capital expenditure on energy conservation incurred in the carrying on of a business. The Commissioner argued that deriving income from rents and interest was not a business. The High Court held that the taxpayer was carrying on a business, quoting several overseas cases that had concluded that negotiating leases and collecting rents from properties gave rise to a business.
79. Whether property leasing constitutes a business is illustrated in Example | Tauira 6.

37 *Dick v CIR* (2002) 20 NZTC 17,961 (CA).

38 At 17,973.

39 *Case G44* (1985) 7 NZTC 1,170 (TRA). See also *Case 2/2012* [2012] NZTRA 02, (2012) 25 NZTC 1,014 and *Case 8/2013* [2013] NZTRA 08, (2013) 26 NZTC 2,007.

40 This would now be subject to the residential rental ring-fencing rules in subpart EL.

41 At 1,173.

42 *Case L102* (1989) 11 NZTC 1,575 (TRA).

43 *LD Nathan Group Properties Ltd v CIR* (1980) 4 NZTC 61,602 (HC).

Example | Tauria 6 – Charitable purposes overseas

TeachAid is a registered charity set up to promote education in low-income countries. The charity derives income from donations as well as rental income from a commercial property in New Zealand consisting of four retail units. The property was donated to the trust by a person who does not retain any interest in the property. The charity engages a property manager to manage all aspects of the property, including leasing the units, maintenance and insurance.

TeachAid wishes to know whether its rental income from the property is exempt from tax in New Zealand.

There are two potentially relevant exemption provisions that apply to a registered charity like TeachAid: ss CW 41 and CW 42. If the rental income is derived from a business, then the question of whether the income is exempt is determined under s CW 42. If the rental income is not business income, the question of whether the income is exempt is determined under s CW 41.

This is particularly relevant for TeachAid because, under s CW 42, an exemption is only allowed to the extent that the charitable purposes are carried out in New Zealand, and TeachAid's charitable purposes are carried out overseas.

It is also noted that under s CW 42(3) a trustee can be treated for the purposes of s CW 42 as carrying on a business if the trustee derives rental income from a property that was transferred to the trust, and the transferor retains an interest in the property. However, this does not apply on these facts. Therefore, the standard business test must be considered.

Applying the business test, the activity is property leasing, which is capable of being a business (*Dick*). The leases of the retail units are ongoing, and the charity receives significant income from the four units. Although the charity engages a property manager to deal with all aspects of the property, the manager is the agent of the charity, so any commitment of time and effort is effectively ascribed to the charity (see [85]). The property is valuable, so represents a significant commitment of money. Finally, the charity intends to profit from the property (albeit for charitable purposes).

Accordingly, it is considered the leasing activity is a business. This means TeachAid's entitlement to an exemption is determined under s CW 42. This means TeachAid's rental income will not be exempt because TeachAid's charitable purposes are carried out overseas.

Person's involvement in a business

80. A question that sometimes arises is whether a person is carrying on a business if they are not themselves involved in carrying on activities that are part of the alleged business.
81. In some cases, it may be difficult to distinguish between a person acquiring services from other persons who may be in business and a person carrying on business themselves by contracting with others to carry out certain tasks.
82. In these cases, a person is more likely to be carrying on a business themselves if they are involved in oversight, organisation or control of the tasks they are paying other people to carry out. If the person has sufficient involvement, the activities of other persons will generally be attributed to the person and considered alongside the person's own involvement when determining whether the person is carrying on business.
83. This is illustrated in the Australian case of *Ferguson v FTC*.⁴⁴ In that case, the taxpayer was a naval officer who intended to buy a grazing property and raise beef cattle when he retired. Several years before he was due to retire the taxpayer entered two agreements. One was with a cattle leasing company and the second was with management company that would care for cattle leased from the first company. The taxpayer had the right to progeny of the leased cattle and made decisions regarding what to do with bull calves. The taxpayer saw the leasing arrangement as a feasible way of building up a herd which he could eventually move to his own property where he could engage in full scale cattle production.

⁴⁴ *Ferguson v FTC* 79 ATC 4,261 (FFC).

84. The court noted that there was evidence of considerable system and organisation in relation to the breeding scheme itself, although most of this was done by the manager. Nevertheless, the court noted the appellant paid for the manager's services. The court also stated that the taxpayer spent a fair amount of his spare time on maintaining familiarity with the progress of the cattle through reports received from the manager and through reading periodicals relating to primary production. The court also noted that the taxpayer began to keep records relating to the breeding programme and maintained a ledger of his receipts and payments. The court also noted a significant proportion of the appellant's income was applied by him under the two agreements. Overall, the court found that the taxpayer was conducting his activities on a commercial basis and was carrying on a business – despite being in the Navy and contracting with others to look after the cattle.⁴⁵
85. Further, if a person has an agency relationship with another person, the person (as principal) will be treated as doing the things that the agent does. Therefore, an agent's activities can be considered in determining whether a person is carrying on a business. This is illustrated in Example | Tauira 6.

Whether a single transaction can give rise to a business

86. A question that occasionally arises is whether a single transaction can give rise to a business.
87. In *Public Trustee*,⁴⁶ Hutchison J said an isolated transaction does not normally constitute a business of dealing, but it is not conclusive:⁴⁷
- ... A person who carries on a business of dealing in land of course buys land for the purpose of selling it at a profit, but it does not follow that, because he buys land for the purpose of selling it at a profit, he carries on a business of dealing in land. The land sold by Marshall was acquired by him in one purchase only. That is a factor to be considered, for an isolated transaction does not normally constitute a business, but it is not conclusive ...
88. In *Mitchell*,⁴⁸ the High Court considered whether a horse breeding activity was a business of dealing in personal property under (what is now) s CB 5. Greig J said:⁴⁹
- I turn then to the three limbs of the subsection, and the first is whether this is a business. **It is a single transaction and clearly was the first transaction by the objectors. It is accepted, as it must be, that a single transaction can be within the terms of the subsection a business dealing in such property, and there are a number of authorities which are cited in support of that.** Moreover, the horse-breeding industry involves rather infrequent transactions and there may be very few in any given business. The operation of one brood-mare producing a foal every year would still be a business as much as the substantial stud with several mares and sires producing numerous progeny for sale each year. **But it must be accepted that a single and first transaction is less likely to be treated as the part of a business.** [Emphasis added]
89. In *Case E99*,⁵⁰ the taxpayer salvaged abandoned agricultural equipment from a property, restored and sold it in four lots, mostly to a related party. The taxpayer argued that the isolated transactions or “one particular act never to be repeated” are normally excluded from the concept of business. Judge Barber accepted that an isolated transaction does not constitute a business but due to the systematic effort of the taxpayer over a six-month period was in “no doubt whatsoever” that there was an undertaking carried on for pecuniary profit.⁵¹
90. In *AAA Developments (Ormiston) Ltd*,⁵² Gendall J confirmed that the taxpayer, which was incorporated for the purpose of developing a single block of land into a significant number of retail units, residential apartments and car parks, was in business.
91. In summary, in determining whether a single transaction gives rise to a business, each situation will depend on its own facts and an application of the *Grieve* factors. This is illustrated in Example | Tauira 7.

45 Comparisons might be drawn between this case and Example | Tauira 1, where Zaid keeps five cattle on a small rural property and the conclusion is he is not carrying on business. However, there are important differences between *Ferguson* and Example | Tauira 1. For instance, in *Ferguson*, the taxpayer's cattle were being managed together with other cattle in a larger scale grazing operation.

46 *Public Trustee v CIR* [1961] NZLR 1,034 (HC).

47 At 1,038.

48 *Mitchell v CIR* (1987) 9 NZTC 6,033 (HC).

49 At 6,037.

50 *Case E99* (1982) 5 NZTC 59,532 (TRA).

51 At 59,539.

52 *AAA Developments (Ormiston) Ltd v CIR* (2015) 27 NZTC ¶22-026 (HC) (see further at [115]).

Example | Taura 7 – One-off property development

Lakefront Limited is a special purpose company incorporated to undertake a small property development involving acquiring a block of bare land and building a single residential house on it for the purpose of sale. The combined cost of the land and house is \$1.2m and the development takes two years to complete. The company wants to ensure its expenditure on the development is deductible under s DA 1.

In terms of the *Grieve* factors, the company has a clear intention to profit from the development. Property development is an activity that can give rise to a business. The commitment of time, money and effort is significant, as the development takes two years from start to finish and costs \$1.2m. However, the scale of operations and volume of transactions is low, as the development consists of building a single residential house and will result in a single sale of that property. The company also has no pattern of activity as it is a special purpose vehicle.

In weighing up the *Grieve* factors, it is considered that the company is not carrying on a business. Although the commitment of time and money is significant, the scale of operations and volume of transactions is too low to give rise to a business.

Despite this conclusion, the company's expenditure will nevertheless be deductible under s DA 1(1)(a) as the company will be taxable on the proceeds of sale under s CB 6.

Whether a person can carry on multiple businesses

92. Another issue that arises is whether a person can carry on multiple businesses or carry on a business while having a full-time job. This usually arises where an individual already has an existing full-time job or business and begins to carry on a new activity. The issue is important as it may determine whether amounts arising from the new activity are taxable.
93. In *Stockwell*, the Court of Appeal considered whether the taxpayer, a structural engineer, was carrying on a business of buying and selling shares. *Hardie Boys J* confirmed that a taxpayer may have two or more businesses.⁵³
Whether a particular activity amounts to a business is a matter of fact and degree, but the continuity and extent of the activity must be important considerations, if not the dominant considerations. Plainly the activity need not be the taxpayer's sole or even principal activity. **A person may have two or more businesses. One may be major, the other or others minor, but all may still be businesses.** [Emphasis added]
94. However, in a separate judgement, *Cooke P* said that when a taxpayer (a natural person) has a full-time occupation, is retired or unemployed, and engages in a modest amount of activity, the presumption should be against a business.⁵⁴
... When a taxpayer has a full-time occupation and devotes some of his spare time to stock exchange speculation, one should be slow, I think, to find that he has gone as far as to embark on a business. Usually it would be an artificial use of language. The same applies to a retired or unemployed person who engages in a modest amount of buying and selling shares. In such cases the presumption should be against a business.
95. In *Case L19*,⁵⁵ Judge Barber accepted that the taxpayer, a medical doctor, was carrying on a small farming business. The taxpayer worked steadily on the farm each weekend, one afternoon during the week and for most of his holidays. Judge Barber regarded the time and effort commitment as quite substantial.
96. Similarly, in *Case L57*,⁵⁶ Judge Barber accepted that the taxpayer was in business both as a farmer and a professional artist.
97. In summary, depending on the facts, it is possible for a person to carry on more than one business. However, where the natural person has a full-time occupation, is retired or unemployed, and devotes a modest amount of time to the other activity, there will be a presumption against a business.

⁵³ At 9,194.

⁵⁴ At 9,194.

⁵⁵ *Case L19* (1989) 11 NZTC 1,125 (TRA).

⁵⁶ *Case L57* (1989) 11 NZTC 1,326 (TRA).

A company may more readily be found to be in business than an individual

98. A company may more readily be found to be in business than an individual. The Privy Council in *Rangatira*⁵⁷ stated at 12,730:

... At one stage in their respective arguments, counsel for both parties took up extreme positions. Thus for the appellant, Mr Underhill QC advanced the contention that there could be no question of liability under s 65(2)(a) since the holding of investments did not constitute the carrying on of a business, and therefore the appellant fell outside the scope of the charge. This is a novel proposition, and one which their Lordships have no hesitation in rejecting. It may well be that in the case of individuals or trustees the holding of investments would very rarely amount to the carrying on of a business. It may well be, therefore, that, if the investments held by the appellant had instead been held by the various bodies of trustees who made up the majority of its shareholders, there would have been no scope for the operation of s 65(2)(a). But the interposition of the appellant made all the difference. The objects clause of the appellant is drawn in conventionally broad terms and authorises it to carry on a range of businesses which embraces almost the whole conceivable gamut of commercial activities. The authorities, to some of which reference must be made, contain a number of instances in which investment holding companies, no less than investment dealing companies, have been treated as carrying on a business for taxation purposes, and their Lordships feel no doubt about the correctness of such treatment.

99. Similarly, it has been stated that any gainful use to which a company puts its assets to make a profit for its shareholders, on its face, amounts to carrying on a business.⁵⁸ However, any presumption as to the existence of a business is rebuttable.
100. The same test outlined in *Grieve* will apply to a company as is applied to an individual or a trustee. Differences may naturally arise in the application of the test, as a company may not have competing non-business purposes like an individual would and the establishment and maintenance of the company may provide some evidence of a profit-making intention.
101. An example of a company that may not be carrying on a business is a company that is established and maintained as a charity. Although such companies can carry on businesses to fund their charitable activities, the existence of a business would not be presumed.⁵⁹

The scope of a business

102. The scope of a business (including the type of business and the various activities carried on in the business) can be important in determining whether income is taxable under s CB 1 and expenditure is deductible under s DA 1(1)(b).

Scope can affect the determination of income

103. For income purposes, an amount a person derives **from** a business is income of the person (s CB 1). In *AA Finance Ltd*, Richardson J said:⁶⁰

... A transaction may be part of the ordinary business of the taxpayer or, short of that, an ordinary incident of the business activity of the taxpayer although not its main activity. A gain made in the course of carrying on the business is thus stamped with an income character.

104. The taxpayer in *AA Finance* provided motor vehicle finance to its members. It was required to hold prescribed levels of government stock for capital adequacy purposes. The issue was whether proceeds from the realisation of the government stock were taxable. The taxpayer argued that the government stock represented an investment separate from and unconnected to its ordinary trading activities.
105. Richardson J described the business of the taxpayer as that of a finance company and said the acquisition and holding of government stock was a necessary incident of that business and, further, its private sector and public sector (ie, government stock) lending were not separate activities.
106. It follows that the scope of a business may be an important factor in determining whether an amount of income arises as part of the ordinary operations of that business or as an ordinary incident.

⁵⁷ *Rangatira Ltd v CIR* (1996) 17 NZTC 12,727 (PC).

⁵⁸ *American Leaf Blending Co Sdn Bhd v Director-General of Inland Revenue* [1979] AC 676 (PC).

⁵⁹ See also IS 24/08: Charities – business income exemption *Tax Information Bulletin* Vol 36, No 10 (November 2024): 3

⁶⁰ *AA Finance Ltd v CIR* (1994) 16 NZTC 11,383 (CA) at 11,391.

Scope can affect the determination of deductions

107. The scope of a business can also be important in determining whether expenditure is deductible under s DA 1(1)(b).
108. For deduction purposes, an amount of expenditure or loss must be incurred **in the course of carrying on** a business under s DA 1(1)(b). This is referred to as the nexus test. The scope of a business is particularly important in determining whether expenditure relating to the commencement of a new or separate business, or the cessation of a business, is deductible.
109. Note that even if the nexus test is satisfied, a deduction may not be available. This is because it is also necessary to consider whether a general limitation applies under s DA 2. For example, expenditure is not deductible if it is of a private or domestic nature (s DA 2(2)).
110. For a new business, a question about the deductibility of feasibility expenditure might arise. The position on feasibility expenditure was summarised by the Supreme Court in *Trustpower* as follows:⁶¹
- Section DA 1 denies deductibility to feasibility expenditure for a new, or an entirely separate, business venture which is not underway at the time the expenditure is incurred. If activities are undertaken to decide whether or not to enter a business (as against, as in this case, in the course of a taxpayer's existing business), the expenditure will lack the required nexus to a business and s DA 1 will not be satisfied.
111. In brief, preparatory expenditure relating to a new or entirely separate business venture that is not yet underway is not deductible.
112. If a person has an existing business and is investigating a new business opportunity, it is particularly important to understand the scope of the existing business to understand whether the new opportunity is an extension of the existing business or an entirely new business. Preparatory expenditure relating to an entirely new and separate business that is not yet underway is not deductible.
113. In *Case L74*,⁶² the taxpayers, who carried on a business of property development, sought to deduct travel expenditure incurred travelling to the Cook Islands to investigate the purchase of land from which they could run a motel. The taxpayers argued that the expenditure related to an extension of their existing business, so was deductible. Judge Barber held that while property development was wide in scope, the expenditure was linked to the creation of a new business as moteliars and was preparatory in nature.
114. In contrast, in *Case S39*,⁶³ the taxpayer was described as being in the business of media and entertainment production, which led the Taxation Review Authority to conclude that expenses incurred on the investigation and formulation of media projects were incurred as part of the taxpayer's ordinary business operations.
115. The scope of a business was relevant in a cessation context in *AAA Developments (Ormiston) Ltd*. In that case the taxpayer entered into a sale and purchase agreement to buy land for development purposes in 2006 subject to the vendor obtaining resource consent. By 2008 the vendor had not obtained consent, and the taxpayer decided not to continue with the development. This led to litigation between the parties as they tried to variously cancel and enforce the contract. The taxpayer sought to deduct expenditure incurred in relation to the litigation. The Commissioner argued that the taxpayer's business had ceased from 2008. The taxpayer argued (among other things) that because its purposes were not constrained by a constitution its business included making "any form of income or profit in relation to the land", such that the litigation constituted a continuation of its business. Gendall J rejected the taxpayer's argument on other grounds but observed that the argument was unsupported because the taxpayer's intention was only ever to develop the land.
116. For a detailed discussion of the scope of a business in the context of feasibility expenditure, see **IS 17/01** Income tax - deductibility of feasibility expenditure.⁶⁴

When a business commences

117. The question of when a business commences is important because it will usually determine the first moment a deduction can be claimed under s DA 1(1)(b). A taxpayer may incur costs in setting up a business including legal fees, training and advertising costs. Setup costs incurred before the business commences will generally not be deductible.

⁶¹ *Trustpower Ltd v CIR* (2016) 27 NZTC 22,061 (SC) at 29,169.

⁶² *Case L74* (1989) 11 NZTC 1,431 (TRA).

⁶³ *Case S39* (1995) 17 NZTC 7,264 (TRA).

⁶⁴ IS 17/01: Income tax – deductibility of feasibility expenditure (interpretation statement, Inland Revenue, 23 February 2017).

118. One exception to this is interest incurred by a company. For most companies, interest is deductible under s DB 7, without having to satisfy the nexus test under s DA 1. This means that for these companies, pre-commencement interest expenditure will be deductible.
119. The issue of when a business has commenced has been considered in both New Zealand and overseas cases.
120. In the English case *Birmingham*,⁶⁵ Rowlatt J concluded that the taxpayer, a manufacturer of meat by-products, had not commenced business until the date it started to receive raw material and produce finished products. Until then, all its actions were merely preparatory to the commencement of business; it was in the process of “getting ready”.
121. *Birmingham* was cited by Barker J in the New Zealand Court of Appeal decision *Duff*,⁶⁶ as being authority for the proposition that a business does not commence until the plant is ready and the owner is ready to commence dealings in the articles from which the owner is to derive profit; preparatory activities do not constitute the running of a business.
122. *Birmingham* was also confirmed by the Court of Appeal in *Calkin*, where Richardson J noted the difficulty in distinguishing between transactions that are preparatory to the commencement of business and those that occur once the business has begun. He concluded:⁶⁷
- Clearly it is not sufficient that the taxpayer has made a commitment to engage in business: he must first establish a profitmaking structure and begin ordinary current business operations.
123. *Calkin* was applied in the High Court decision of *Stevens & Stevens*.⁶⁸ In *Stevens & Stevens*, Gallen J also noted that it is not always easy to establish when a business commences and said:⁶⁹
- Preliminary investigations will clearly not be enough, nor will the expenditure of capital requirements in order to enable the business to be carried on, see *Birmingham and District Cattle By-Products Company Limited v Commrs of IR*. The business must involve trading.
124. Gallen J went on to consider the Canadian case *MP Drilling Ltd*⁷⁰ where it was held that a business had commenced when the permanent structure, the market and the products all existed, and the efforts of the respondent were directed to bringing them together with a resultant profit to it.
125. Despite the requirement that the income-earning process must have begun, there are cases that indicate it is not necessary for a taxpayer to have derived any income from an activity for a business to have commenced. For example, in *Eggers*,⁷¹ Richardson J concluded that a deduction may be allowed for expenditure incurred even though no income was derived in the year in which the expenditure was incurred. However, he emphasised that it was necessary for a business to have commenced.
126. The ultimate failure or abandonment of all or part of an activity does not necessarily indicate that a business was never commenced.⁷²
127. In summary, key factors to consider in determining whether a business has commenced are whether:
- the profit-making structure has been established; and
 - ordinary current business operations have begun.
128. The profit-making structure and the current business operations could look very different depending on the type of business involved. For example, for a manufacturing business, a profit-making structure may not be established until machinery has been set up and the ordinary current business operations may not begin until finished products are being produced. For a property development activity, the profit-making structure and current business operations might look quite different.⁷³

65 *Birmingham & District Cattle By-Products Co Ltd v Inland Revenue Commissioner* (1919) 12 TC 92 (KB).

66 *Duff v CIR* (1982) 5 NZTC 61,131 (CA) at 61,144.

67 At 61,786.

68 *Stevens & Stevens v CIR* (1989) 11 NZTC 6,001 (HC).

69 At 6,006.

70 *Minister of National Revenue v MP Drilling Ltd* [1976] CTC 58 (FCA).

71 *Eggers v CIR* (1988) 10 NZTC 5,153 (CA). See also *Stevens & Stevens v CIR*, Case M68 (1990) 12 NZTC 2,384(TRA), *Slater v CIR* (1996) 17 NZTC 12,453 (HC) and *Case T25* (1997) 18 NZTC 8,160 (TRA).

72 See, for example, *Goodman Fielder Wattie Ltd v FCT* 91 ATC 4,438 (FCA) and *Whitfords Beach Pty Ltd v Federal Commissioner of Taxation* 83 ATC 4,277 (FCAFC).

73 See *Whitfords Beach Pty Ltd v FCT* 83 ATC 4277 (FCAFC) and *AAA Developments (Ormiston) Ltd v CIR* [2015] NZHC 2,318; (2015) 27 NZTC 22,026.

129. For further discussion of business commencement in the context of:

- feasibility expenditure, see **IS 17/01**: Income tax - deductibility of feasibility expenditure;
- bloodstock breeding, see **QB 22/07**: Income Tax and Goods and Services Tax – Treatment of bloodstock breeding;⁷⁴ and
- content creators, see **IS 21/08** Content creators - tax issues at [85].⁷⁵

See also Example | Taura 8 and Example | Taura 9.

Example | Taura 8 – Starting a small service business

Graeme wishes to become self-employed, so he takes steps to set himself up as a bookkeeper. He retires from his previous employment and spends April and May converting an existing sleepout at his property into a home office. Once the conversion is complete, Graeme spends June acquiring the necessary office equipment and supplies and setting up his office. On 2 July, he starts seeking clients and is available to start providing bookkeeping services. Seeking clients involves posting advertisements on social media and entertaining. On 5 August, Graeme obtains his first client but must wait until 12 September before he receives sufficient information from his client to begin work. There is only enough work at this point to keep Graeme busy two days a week. On 15 October, Graeme raises his first invoice. In November, Graeme obtains two further clients, and by December he is working full time as a bookkeeper.

Graeme wishes to claim deductions under s DA 1 for expenses incurred in painting his home office, buying stationary and entertaining prospective clients and for office overheads (including a portion of rates, insurance and mortgage interest) and depreciation on his office equipment. The issue is when his business commenced.

The required profit-making structure for Graeme's business is in place by the end of June when he finishes setting up his home office. Graeme's ordinary business operations begin on 2 July because Graham was ready to start providing bookkeeping services at that time and in Graeme's situation seeking new clients will be part of his ordinary business operations. Even after December, by which time he is working full time, he may need to seek new clients if old clients are lost.

It follows that Graeme's business commenced on 2 July. The fact Graeme did not start keeping books straight away and had not yet raised an invoice does not affect this conclusion.

This commencement date means that any expenditure incurred or depreciation loss arising before 2 July is not deductible under s DA 1.

Example | Taura 9 - Product design business interrupted

Fadi is a well-regarded product designer with 15-years' experience who wants to start out in business on his own designing homeware. He researches the market for a range of homeware products he has in mind. Based on his research, he thinks he can design products to licence to manufacturers. He creates a business plan and approaches private investors for funding that he will need to cover expenditure while starting out – he expects to make a loss in the first two years of business. After securing the funding, he resigns from his current employment. He then sets up a company, searches for an appropriate office and workspace and advertises for employees. The company then employs two staff, sets up the office and workspace and begins work on the first product designs. The company's business plan will see the company working on a pipeline of product design projects which it will then licence to manufacturers. The company plans to be able to market initial designs to manufacturers and enter licencing contracts six months after setting up the office.

However, three months after setting up the office, Fadi is involved in an accident, and the business cannot continue. The company's accountant wants to know whether expenditure incurred by the company is deductible. The accountant is unsure whether the business had commenced, given no contracts had been entered or income derived.

⁷⁴ QB 22/07: Income tax and goods and services tax – treatment of bloodstock breeding *Tax Information Bulletin* Vol 34, No 9 (October 2022): 22.

⁷⁵ IS 21/08: Content creators – tax issues *Tax Information Bulletin* Vol 33, No 10 (November 2021): 33 at [85].

The business commenced when the company set up the office and workspace and started product design. The product design was part of the current business operations of the company. Accordingly, expenditure, including staff and office costs incurred during the three months the business was carried on could potentially qualify for a deduction. However, consideration may need to be given to whether the expenditure is capital expenditure and how the depreciation rules apply in this situation to any depreciable property.

When has a business ceased

130. The question of when a business has ceased is important because it generally determines the last moment when expenditure can be deducted for tax purposes under s DA 1.
131. In *Case U29*, Judge Barber said it was settled law that post-cessation expenditure did not meet the criteria for deductibility:⁷⁶
- It is also settled law that post-cessation expenditure does not meet the criteria of s 104**, and the various authorities for that seem to rely on the words of Latham CJ of the High Court of Australia in *Amalgamated Zinc (de Bavay's) Ltd v FC of T* (1935) 54 CLR 295 at p 303:
- “So it has also been held that expenditure which has a direct relation to income of a past year can be deducted in a later assessment year where it is of such a character that, in a continuing business, it must be met from time to time as part of the process of gaining assessable income ... But even this benevolent construction cannot assist the taxpayer in a case like this, **where there has been a complete cessation of the income-producing operations out of which the necessity to make the outgoing arose.**” [Emphasis added]
132. A common type of post-cessation expenditure is interest expenditure. A deduction for interest charged on a loan is only available in an income year to the extent the loan amount has been used in the business during that income year. With the exception of some companies, interest expenditure paid on a loan after the business ceases is not deductible – even if the loan amount was used in the business before it ceased. This was the conclusion reached in *Case L89*⁷⁷ and *Case N7*.⁷⁸
133. This is based on what is described as the “use test”. Under the use test, interest is deductible if it is paid on capital (loan principal) used in the production of assessable income. Importantly, the question is how the loan is being used in the income year for which the interest deduction is being sought. A deduction is only available for an income year if the loan capital is still being used in the business in that income year. The use test can be traced back to cases such as *Pacific Rendezvous Ltd*,⁷⁹ *Eggers*⁸⁰ and *Brierley*.⁸¹
134. For some companies, interest expenditure is deductible under s DB 7 without having to establish a nexus or connection with the derivation of income. This means that interest expenditure can continue to be claimed by these companies post cessation.
135. The position in New Zealand on the deductibility of expenditure post-cessation differs from the position in other countries. In Australia, for example, the courts allow deductions after a business has ceased, provided that “the occasion” for the expenditure is to be found in a transaction entered into in the carrying on of the business (ie, before cessation) for the purpose of producing assessable income.⁸² Given that the Australian cases were heard by the full Federal Court of Australia, the Australian case law might be influential in any future New Zealand judicial consideration of the issue. However, at the moment, the New Zealand position is different from that in Australia.
136. A business ceases when the activities cease or are no longer at a sufficient scale to be considered a business, or when there is no longer an intention to make a profit. This usually occurs when a business is winding up, but the question may also arise where a business downscales or temporarily ceases. Each of these contexts is discussed below.

⁷⁶ *Case U29* (2000) 19 NZTC 9,273 (TRA) at [50].

⁷⁷ *Case L89* (1989) 11 NZTC 1,508 (TRA) at 1,512.

⁷⁸ *Case N7* (1991) 13 NZTC 3,048 (TRA) at 3,051.

⁷⁹ *Pacific Rendezvous Ltd v CIR* (1986) 8 NZTC 5,146 (CA).

⁸⁰ *Eggers v CIR* (1988) 10 NZTC 5,153 (CA).

⁸¹ *CIR v Brierley* (1990) 12 NZTC 7,184 (CA).

⁸² See *FCT v Riverside Road Pty Ltd (in liq)* 90 ATC 4,567 (FFC), *Placer Pacific Management Limited Pty v CT 95* ATC 4,459 (FFC), *FCT v Brown* 99 ATC 4,600 (FFC), and *FCT v Jones* 2002 ATC 4,135 (FFC). *Case 17/2014* (2014) 26 NZTC 2,027 (TRA) does not provide clear authority for following the approach taken in the Australian cases. In *Case 17/2014*, the TRA was not required to decide whether post-cessation expenditure was deductible because the TRA held that there was an insufficient nexus in any event.

Winding up a business

137. When a business is in the process of winding up, there will come a point at which there is either no intention to make a profit, or the level of activity is too low to constitute a business.
138. In *Case F31*,⁸³ Judge Bathgate held that the taxpayers no longer had an intention to profit in the context of winding up a business. The taxpayers, a husband-and-wife partnership, acquired land intending to establish an orchard. They initially planted an onion crop on the land; it failed. Subsequently, and before acquiring any fruit trees or vines, the taxpayers decided to sell the land. Before the sale went through, the land was planted in maize. The taxpayers sought to deduct losses from the onion crop as well as expenses incurred planting the maize against their other income. Judge Bathgate said:⁸⁴
- The objectors were carrying on the farming partnership venture for the purpose of obtaining an excess of income over expenditure. They were carrying on the venture for pecuniary gain. I am satisfied that was their purpose until at least 29 October 1979. ...
- When the objectors decided to sell the land, or endeavour to sell the land, on 29 October 1979 I am not satisfied on a balance of probability that their intention to make a profit from the farming partnership continued. In this regard I again refer to "profit" in the sense of excess of income over expenditure, and not to a capital profit. In my view the objectors have proved no more than from that date they continued with the maize planting and growing as an aid to their sale of the land.
139. In summary, Judge Bathgate concluded that the taxpayers ceased to have an intention to profit from the date they decided to sell the land and that the maize was merely planted to aid the sale of the land.
140. See also *AAA Developments (Ormiston) Ltd* (discussed at [115]) in which the High Court held that the taxpayer ceased to have a profit-making intention from the date it decided to abandon a property development.
141. In *Case L89*,⁸⁵ Judge Barber found that a hotel business had ceased when the hotel lease and chattels were sold. The taxpayer acquired a hotel business funded in part by a loan from the vendor. The business was not as profitable as represented, and the taxpayer ceased making interest payments under the loan. The vendor appointed a receiver who operated the business on the taxpayer's behalf for a time before selling the business. For the following two years the taxpayer was involved in litigation against the vendor and collecting trade debts. The taxpayer sought to claim interest deductions over that period. Judge Barber said:⁸⁶
- ... I find that the trading activity of the objector ceased on 9 October 1983 when the hotel lease and chattels were sold to new licensees. Although the receivership was terminated on 17 December 1985, by the beginning of the 1985 income tax year there was no business activity taking place on behalf of the objector company. True, **the recovery of debts and tidying up of the affairs of a business can be of such a degree as to amount to a continuation of the previous trading business, but not usually.** That issue must always be one of fact and degree in any particular case. Here, there was very little such activity in 1985 and 1986. **I do not accept as a general proposition that, for income tax purposes, a business continues so long as it has debts which result from that business.** [Emphasis added]
142. In summary, Judge Barber concluded there was insufficient activity to constitute a business after the sale of the hotel business. However, he acknowledged that depending on the facts the recovering of debts and tidying up the affairs of a business may amount to a continuation of the business, but not usually.
143. In *Case U29*, which concerned the deductibility of a settlement payment arising from litigation following the sale of a business, Judge Barber revisited the above conclusion and said:⁸⁷
- ... Since [*Case L89*], my approach to that situation has slightly mellowed in terms of my perception of current commercial practice. It now seems to me that the tidying-up of the affairs of a business could often mean the continuance of the business for income tax purposes for a reasonable period beyond cessation of trading, but one needs to examine the particular facts of the case to ascertain whether or not the business terminated when trading ceased.
144. In summary, Judge Barber confirmed that, depending on the facts, the tidying up of the affairs of a business for a reasonable period beyond the cessation of trading could mean the continuance of the business.

⁸³ *Case F31* (1983) 6 NZTC 59,712 (TRA).

⁸⁴ At 59,719.

⁸⁵ *Case L89* (1989) 11 NZTC 1,508 (TRA).

⁸⁶ At 1,511.

⁸⁷ At 9,280.

145. In conclusion, the question of when a business ceases in the context of winding up depends on the facts. The sale of a business or a decision to sell or abandon could indicate that there is no longer a profit-making intention. Alternatively, the scale of activity may become too low to sustain the continued existence of a business. Where trading has ceased, a business may nevertheless continue for a reasonable period so its affairs can be tidied up.

Downscaling a business

146. Some businesses choose to downscale their operations until trading conditions improve by reducing staff numbers or hours of operation. If there is still an intention to make a profit and sufficient operational activity (relevant to that type of business and current market conditions), then it is likely a business is still being carried on and any expenditure or loss incurred can be deducted.
147. In *Case F131*,⁸⁸ Judge Barber said it is not necessarily correct that if through adversity (or any other reason) the major part of an enterprise is sold off and the balance continued for a time, then the owners are no longer in business.
148. Despite this, a point will come where the downscaling is to such a degree that it indicates the business has ceased.
149. In *Case J78*,⁸⁹ an elderly couple decided to reduce the area of their farm from 50 acres to 4 acres to reduce costs and alleviate the physical burden of farming. They also decided to diversify their farming from annual crops to longer-term crops that required less effort. The longer-term crops were not readily available, so the couple continued to farm as usual, but only on the 4 acres. They farmed this way, knowing there would be little chance of a profit, and worked part-time jobs to supplement their income. The couple claimed deductions for business losses over the period. The Commissioner disallowed the claim on the basis that they had not been carrying on a business. Judge Barber held that by farming on a reduced scale and with the knowledge that they would not make a profit, the taxpayers could not be regarded as carrying on a business.

Temporary cessation

150. When applying the business test, the courts have drawn a distinction between a temporary cessation of business (where the business activities have temporarily ceased or been suspended but will recommence) and cessation with the possibility of recommencement (where business activities have ceased, and it is not certain they will recommence). Deductions are usually allowed for temporary cessation but not for cessation with the possibility of recommencement.
151. This distinction was explained in *Case F73*.⁹⁰ The taxpayer company was a partner in a fishing venture. In 1979, the skipper resigned, and the boat stopped being used for fishing, although the partners continued to look for a new skipper. In 1980, the boat was removed from the water to reduce overheads and sale became a possibility. The boat was sold a year later. The taxpayer claimed a deduction for expenses incurred in the 1981 income year, arguing that at this stage, there was merely a temporary cessation of the fishing venture. They relied on attempts (that came to nothing) to set up share fishing or leasing arrangements with the boat.
152. Judge Barber held that by 1981 the business had ceased to operate, and the partners were biding their time over the best course of action to take. This was not a temporary cessation, but a cessation with the possibility of recommencement.⁹¹

The source of income from fishing no longer existed well before 1 April 1980. I consider that there was not merely a temporary cessation of income earning operations in the partnership. There was a cessation with the possibility of recommencement if a suitable operating structure could be worked out with a third party. [Emphasis added]

⁸⁸ *Case F131* (1984) 6 NZTC 60,200 (TRA) at 60,204.

⁸⁹ *Case J78* (1987) 9 NZTC 1,459 (TRA).

⁹⁰ *Case F73* (1983) 6 NZTC 59,931 (TRA).

⁹¹ At 59,935.

153. In *AAA Developments (Ormiston) Ltd* (discussed at [115]), Gendall J rejected the taxpayer's argument that its business had only temporarily ceased. The Commissioner argued that the taxpayer's business had ceased from the time it decided not to continue with the property development. The taxpayer argued, among other things, that its business had only temporarily ceased because it had not abandoned all expectation of resuming the property development. Gendall J concluded:⁹²

... This leads to the conclusion, in my view, that from 24 July 2008 AAA no longer had any profit making intention. The factors favouring this conclusion are:

- (i) the development was not proceeding (due to first, AAA's and Ormiston's attempts to extricate themselves from the purchase agreement, seen as an onerous contract, secondly, the subsequent litigation and, thirdly, the economic downturn);
- (ii) from that point forward, there was no prospect of deriving assessable income, with efforts being directed towards recuperating losses and winding up of the business.

154. In summary, Gendall J rejected the taxpayer's argument on the basis there was no longer any profit-making intention.

155. The above cases can be contrasted with the Queensland Supreme Court decision in *Queensland Meat Export Co Ltd v FCT*.⁹³ In that case, the taxpayer operated meat works in two locations. One of the works was closed for three years because of competition from a new abattoir in the area, but it was intended that it would reopen once conditions improved. However, after three years, the directors decided to advertise the closed works for sale as a going concern. The issue was whether expenditure incurred in relation to the closed works such as insurance, rates, security and depreciation was deductible during the three-year period. Douglas J held that the cessation of business was merely temporary until the decision to sell was made.⁹⁴

I consider that the establishment of the abattoir in Brisbane resulted in business competition which compelled the appellant to close its works at Brisbane. Such closure was at first temporary. **The works and plant were kept in good order and condition in the hope that they might be profitably used at some future date.** When the decision to offer them for sale was made on 5th July, 1934, such hope had vanished, but in the expectation of sale the money expended until the end of November was properly expended in keeping the works and plant in good order and condition. **I think it is one of the incidents of a business of this kind that competition or other adverse conditions may compel the owner to close down [a] portion of its plant for an indefinite period. It is an ordinary business precaution that during such period the works and plant should be retained so far as possible in good working order whether the ultimate result be that they should again be opened or that they should be sold or eventually dismantled.** It appears to me that it is an incident of all competitive manufacturing works and plants that some of them may succumb temporarily or finally to their more successful rivals. **The question whether the cessation of operations is merely of a temporary nature or is one which has reached the final stage is difficult to answer.**

In the present case I have come to the conclusion that up to the 5th July, 1934, the cessation was of a temporary nature. After that date, seeing that the plant had merely been offered for sale and not sold, I think the appellant may be considered as holding the plant for sale in the first instance and for possible use if some turn of the tide came.

156. In summary, the court in *Queensland Meat* accepted that it may be an ordinary incidence of business to shut down part of its operations for an indefinite period. However, drawing the line between a temporary cessation and cessation with the possibility of recommencement can be difficult.

157. Ultimately, whether a business has ceased is a question of fact in each case. However, it is easier to argue a business is being carried on where it is well established and has kept its business structure and assets in place. Properly maintaining assets and expending time and effort on a relaunch also support the argument that a business was continuing despite a hiatus.

158. For a more detailed discussion of the distinction between temporary cessation and cessation with the possibility of recommencement see **IS 21/04** Income tax and GST – deductions for businesses disrupted by the COVID-19 pandemic.⁹⁵

159. The deductibility of expenditure on the winding down of a business is illustrated in Example | Tauira 10.

⁹² At 28,746.

⁹³ *Queensland Meat Export Co Ltd v FCT* (1939) 5 ATD 176 (QSC).

⁹⁴ At 180.

⁹⁵ IS 21/04: Income tax and GST – deductions for businesses disrupted by the COVID-19 pandemic *Tax Information Bulletin* Vol 33, No 9 (October 2021): 8.

Example | Taura 10 – Winding up a business

Capital Foods Limited owns and operates a popular central city café. However, due to the increase in people working from home and a decrease in nearby parking spaces, clientele has dropped off and the business is no longer viable. The owners make the difficult decision in May to close the café from the end of June.

The company engages its lawyers to advise on staff redundancies and negotiate a break of its lease.

The café's last day of trading is 30 June. No income arises after that date. The company does its final pay run the following week, paying accrued wages, holiday pay and redundancy entitlements.

A break fee is paid to the landlord in August, and the company incurs expenditure removing its plant and equipment and cleaning the premises.

The company's equipment is advertised for sale on an online auction site in August. The coffee machine sells quickly at a loss, but the chairs, tables and crockery remain unsold in November. The company continues to incur storage costs and ultimately pays for the unsold items to be taken to the dump in December.

The company has an outstanding loan, which it is unable to repay immediately. The company will be repaying the loan (and incurring interest) for some time.

The company's owner wonders whether the company can deduct its staff costs, the lease break fee,⁹⁶ cleaning costs, the loss on sale of the coffee machine, storage costs, equipment disposal costs and interest.

The company ceased to have a profit-making intention from the date it ceased trading (ie, 30 June). However, a business can continue for a reasonable period beyond cessation of trading while its affairs are tidied up. It is considered that the amount of time the company takes to wind down its operations is reasonable in this context, so the expenditure outlined above is deductible.

Because Capital Foods Limited is a company, it is able to continue to claim deductions for interest after the business has ceased (s DB 7 allows a company to claim an interest deduction without being required to establish a nexus between the interest expense and the production of income). However, if Capital Foods Limited wasn't a company, the interest incurred after December would not be deductible.

The difference between a business and a GST taxable activity

160. There are important differences between a business for income tax purposes and a "taxable activity" for GST purposes.
161. Whether a person is carrying on a "taxable activity" is a key concept for determining whether a person is required to register for and charge GST. A taxable activity is broadly defined as an activity that is carried on continuously or regularly, whether or not for profit, that involves or is intended to involve supplies of goods or services for consideration.⁹⁷
162. Although the concept of a taxable activity is similar to the income tax meaning of a business, there are some important differences. In particular, the definition of taxable activity has many prescribed requirements that must be satisfied. In addition, a taxable activity does not need to be carried on for profit, where a business does.
163. Another important difference is that activities connected with the commencement or ending of a taxable activity are treated as being carried out in the course of that activity.⁹⁸ There is no equivalent rule for income tax purposes.
164. It follows that the fact the Commissioner may accept a taxable activity is being carried on for GST purposes does not mean a business exists.
165. For an in-depth discussion of the meaning of taxable activity, see **IS 25/21: GST – taxable activity**.⁹⁹

⁹⁶ Lease surrender payments are deductible under s DB 20C if they satisfy the general permission in s DA 1.

⁹⁷ Section 6 of the Goods and Services Tax Act 1985.

⁹⁸ Section 6(2) of the Goods and Services Tax Act 1985.

⁹⁹ IS 25/21: GST – taxable activity *Tax Information Bulletin* Vol 37, No 9 (October 2025).

Whether there is a business is not determinative of tax

166. The question of whether there is a business will not necessarily be determinative of whether an amount is income or whether a deduction is available. A person may have an income-earning activity that does not fall within the definition of a business. Amounts derived may be included in a person's income under another taxing provision in the ITA, and deductions may be available for expenditure incurred in deriving that income. This is illustrated in Example | Taurira 4 and Example | Taurira 7.

References | Tohutoro

Legislative references | Tohutoro whakatureture

Goods and Services Tax Act 1985, s 6

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QUESTION WE'VE BEEN ASKED

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

QB 25/21: Income tax – Public private partnership projects and business continuity test for losses

Issued | Tukuna: 23 October 2025

This question we've been asked considers whether a major change in the nature of a contractor's business activities occurs under the business continuity test for losses when a public private partnership project moves from a design and construction phase to an operating and maintenance phase.

Key provisions | Whakaratonga tāpua

Income Tax Act 2007 – s IB 3(2)(c) and IB 3(5)(d)

All legislative references are to the Income Tax Act 2007.

Background | Horopaki

Under a standard New Zealand public private partnership (PPP) project, a corporate Contractor or a corporate limited partner of a Contractor (if the Contractor is a limited partnership (LP)) may incur tax losses during the initial design and construction phase (D&C Phase). If there is a material change in the shareholding of the corporate Contractor or corporate limited partner, the relevant entity may need to rely on the business continuity test (BCT) in subpart IB to carry forward its tax losses.¹

One requirement for applying the BCT is that no "major change" in the nature of the company's business activities occurs during the business continuity period, unless it is a "permitted major change".

Question | Pātai

Is there a "major change" in the nature of a PPP Contractor's business activities when the project moves from the D&C Phase to the operation and maintenance phase (O&M Phase)? If there is a major change, is it a "permitted major change"?

Answer | Whakautu

The change from the D&C Phase to the O&M Phase could be a "major change" in the nature of the Contractor's business activities. However, any "major change" will be a "permitted major change" because the services provided in each of the two phases are closely connected due to the economic, legal and financial dependencies of the two phases. Therefore, despite a breach in ownership continuity and the phase change, the corporate Contractor or the corporate limited partner² of an LP Contractor can carry forward its tax losses if it meets the other requirements of the BCT and the avoidance provisions in ss GB 3BA to GB 3BAC do not apply.³

¹ For detailed guidance on BCT refer to IS 22/06: Loss carry-forward – continuity of business activities.

² For simplicity and due to the limited scope of this question we've been asked, it is assumed that the corporate limited partner only undertakes activities relating to the PPP project.

³ For detailed guidance on ss GB 3BA to GB 3BAC, refer to IS 25/14: Income tax – arrangements involving tax losses carried forward under the business continuity rules.

Key terms | Kīanga tau tāpua

BCT means the business continuity test in subpart IB that allows a company to carry forward losses even if an ownership continuity breach has occurred.

Contractor means the special purpose vehicle (which may be a company or limited partnership) contracting with the Crown under the Project Agreement.

D&C Phase means the design and construction of the asset by the Contractor.

O&M Phase means the operation and maintenance of the asset by the Contractor.

PPP means a public private partnership involving the Crown and private sector to design, build and operate and/or maintain an asset under a Project Agreement.

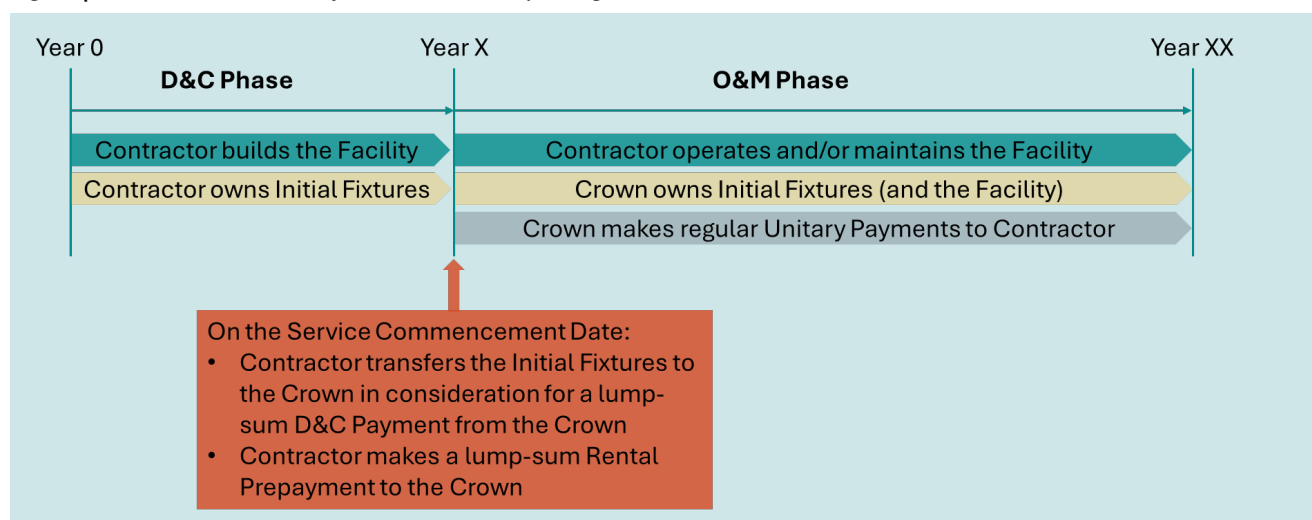
Project Agreement means the standard form Project Agreement the Crown uses for PPPs.

Explanation | Whakamāramatanga

Nature of a PPP

1. A PPP represents a long-term contract for the delivery of a service requiring the construction of a new asset or enhancement of an existing asset. Typically a PPP is financed from external sources on a non-recourse basis, and full legal ownership of the asset is retained (or returned to) the Crown.
2. PPP projects are generally governed by a standard form Project Agreement. The Project Agreement framework has three main components that are relevant to this question we've been asked:
 - the **D&C Phase** when the Contractor designs and constructs the asset (the Facility) for the Crown. Any fixtures the Contractor builds in this phase (the Initial Fixtures) are transferred to the Crown at the end of the phase in return for a lump-sum design and construction payment (D&C Payment);
 - the **Facility lease** between the Contractor and the Crown, under which the Contractor prepays an amount representing the rental the Contractor will pay to the Crown (Rental Prepayment);
 - the **O&M Phase** when the Contractor provides operational and maintenance services for the Facility over a period of approximately 25 years in return for a regular payment from the Crown (Unitary Charge). Broadly, the operational and maintenance services are those services necessary to meet asset management requirements. The services will vary depending on the type of asset being constructed.
3. Figure | Hoahoa 1 depicts the main components described above.

Figure | Hoahoa 1 – Main components of the Project Agreement framework



4. During a PPP project, the shareholding of a corporate Contractor or a corporate limited partner of a Contractor (if the Contractor is an LP)⁴ may sometimes change in the D&C Phase. If this change in shareholding breaches the 49% ownership continuity test, then the relevant corporate entity will not be able to carry forward tax losses incurred before the breach in ownership continuity unless permitted by the BCT.

Carrying forward tax losses

5. The general rule is that a company must satisfy the 49% ownership continuity test to carry forward its tax losses.
6. The BCT acts as a secondary test, permitting a company to carry a loss forward if it has a breach in ownership continuity. One of the requirements to satisfy this test is that there is **no major change** (other than a **permitted major change**) in the nature of the business activities of the company under s IB 3(2)(c).
7. If a breach occurs in the ownership continuity of a corporate Contractor or a corporate limited partner of an LP Contractor during the D&C Phase of a PPP project, to rely on the BCT to carry forward the relevant corporate entity's losses, the transition from the D&C Phase to the O&M Phase must either:
 - not be a major change in the nature of the Contractor's business activities; or
 - if it is a major change, be a permitted major change under s IB 3(5)(d).

Major change

8. Section IB 3(2)(c) states:

Tax loss components for earlier income years carried forward

- (2) Despite the ownership continuity breach, a tax loss component arising in an earlier income year is carried forward to a tax year in a loss balance under section IA 3(4) (Using tax losses in tax year) if—

...

- (c) **no major change** in the nature of the business activities carried on by the company occurs during the business continuity period, other than 1 or more major changes that are permitted under subsection (5);

[Emphasis added]

9. To determine whether a major change has occurred, it is necessary to examine the nature of the business activities the Contractor carries on during the D&C Phase and the O&M Phase. This examination requires considering the following factors:⁵
 - the Contractor's core business processes;
 - the type of products or services produced or provided;
 - the assets factor;
 - significant suppliers or inputs;
 - scale; and
 - the main markets supplied to.
10. Table | Tūtohi 1 provides an example of how the above factors apply. It gives a high-level indicative overview of the relevant factors for a PPP project undertaken to build a highway.

⁴ For guidance on the attribution of partnership business activities to partners, refer to paras [54] to [58] of **IS 25/11: Income tax – Partnerships (including limited partnerships) – general guidance**.

⁵ Para 32 of IS 22/06: Loss carry-forward – continuity of business activities (October 2022) and s IB 3(4).

Table | Tūtohi 1 – High-level overview of the relevant factors for a highway PPP project

Factor	D&C Phase	O&M Phase
Core business processes	Designing and constructing the highway	- Providing ongoing maintenance and repairs - Managing road services such as toll collection and traffic monitoring
Products or services	The completion of the highway (including the delivery of the Initial Fixtures to the Crown)	- Ongoing maintenance services for the highway - Traffic management and monitoring - Road repair and upkeep services
Asset factor	- Construction equipment such as bulldozers, excavators and pavers - Temporary facilities for construction workers	- Maintenance vehicles and equipment for road repairs - Traffic management systems such as cameras and sensors - Tools and equipment for routine maintenance and repairs
Significant suppliers/inputs	- Construction materials such as asphalt, concrete, and steel - Engineering and architectural services - Labour for construction activities	- Maintenance service providers for road repairs and traffic management - Suppliers of repair materials and parts - Traffic monitoring and management service providers
Scale	- Large-scale construction project involving significant resources and workforce - High intensity of construction activities and coordination	- Routine maintenance and operations involving a smaller, more specialised workforce - Lower intensity of activities focused on upkeep and operational efficiency
Main markets	Government	Government

11. The change from the D&C Phase to the O&M Phase could be considered a “major change” under s IB 3(2)(c) because the nature of the services the Contractor provides during the two phases is fundamentally different (as in Table | Tūtohi 1). The D&C Phase involves significantly more complexity, cost and resources to construct the asset compared with the operation and maintenance of the asset during the O&M Phase.
12. However, even if a change is considered to be major under s IB 3(2)(c), a company continues to meet the requirement under that section if the change is a “permitted major change” under s IB 3(5)(d).

Permitted major change

13. Section IB 3(5)(d) states:

- Permitted major changes
- (5) A major change in the nature of the business activities carried on by the company during the business continuity period does not breach the requirement set out in subsection (2)(c) if the major change is –
- ...
- (d) caused by a change in the type of products or services the company produces or provides that involves the company starting to produce or provide a product or service using the same, or mainly the same, assets as, or that is otherwise **closely connected with**, a product or service that the company produced or provided immediately before the beginning of the business continuity period.
- [Emphasis added]

14. Accordingly, to satisfy s IB 3(5)(d), services provided during the O&M Phase must be “closely connected” with services provided during the D&C Phase.
15. The term “closely connected” is not defined in the Act. “Close” in the *Concise Oxford English Dictionary* (12th ed, New York, Oxford University Press) in the context of a connection means strong. One meaning for “connected” as defined in the *Concise Oxford English Dictionary* is joined or linked together. Therefore, the connection between the new product or service and existing products or services needs to be strong. Some examples, as noted in IS 22/06, could include products or services:
 - based on the same underlying technology;
 - that significantly enhance the utility or enjoyment of existing products or services; or
 - that are commonly sold together with existing products or services in order to enhance the sales of those products or services.
16. The services provided during the O&M Phase are “closely connected” with the services provided during the D&C Phase for the following reasons:
 - The Project Agreement incorporates both the D&C Phase and O&M Phase. The Facility constructed during the D&C Phase, including the Initial Fixtures transferred to the Crown, creates the physical infrastructure on which the O&M services are performed. Therefore, the O&M services are inherently linked to services undertaken in the D&C Phase because they are carried out on the very infrastructure that is designed and built during the D&C Phase.
 - Under the Project Agreement, the Contractor must ensure the Facility achieves operational completion by no later than the planned Service Commencement Date. This requirement directly ties the services provided during the D&C Phase to the readiness of the Facility for operational services, highlighting the inherent connection between these phases.
 - The base case financial model integrates the financial planning for both the D&C Phase and the O&M Phase. It includes assumptions and projections that cover the entire lifecycle of the project, ensuring that the financial viability of the operational services is directly linked to the successful completion of the design and construction phases.
 - The Unitary Charge, which is the fee payable by the Crown during the O&M Phase, is calculated from the base case. This charge reflects the financial requirements of both the D&C and O&M Phases, and is expected to recover all of the Contractor’s costs in relation to the project and provide its profit margin for the whole project.
17. Therefore, any major change from the D&C Phase to the O&M Phase under the Project Agreement will be a permitted major change under s IB 3(5)(d). The relevant corporate entity can rely on the BCT to carry forward its tax losses if it meets the other requirements of s IB 3 and if the avoidance provisions in ss GB 3BA to GB 3BAC do not apply.
18. The Commissioner considers the above outcome (that the BCT allows the relevant corporate entity to carry forward its tax losses) applies even if the relevant corporate entity subcontracts the physical work to another party.

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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 25/24: The supply of accommodation in a serviced apartment

Decision date | Rā o te Whakatau: 25 July 2025

Issue date | Rā Tuku: 22 October 2025

Subjects | Kaupapa

This item summarises a private ruling about the supply of accommodation in a retirement village that includes the provision of mandatory services and whether this constitutes the taxable supply of accommodation in a commercial dwelling.

Taxation laws | Ture tāke

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

Summary of facts | Whakarāpopoto o Meka

1. The Applicant is developing a retirement village.
2. The Arrangement is the provision by the Applicant of accommodation in serviced apartments. Along with this accommodation, the Applicant provides mandatory services under a hospitality package.
3. Residents will enter into an occupation right agreement (ORA) for a serviced apartment in the village and will be required to make monthly payments for the provision of care services from the hospitality package.
4. The hospitality package includes morning and afternoon teas, village transport, 24-hour emergency call monitoring, weekly apartment cleaning, a pre-entry health assessment, monthly health checks, organised activities and access to electric vehicles and recreational equipment.
5. The Applicant applied for a private ruling that the provision of accommodation in the serviced apartments with the hospitality package was a taxable supply of accommodation in a “commercial dwelling”.

Issue | Take

6. The main issue considered in this ruling was whether, under s 2(1), the supply of accommodation in a serviced apartment with a hospitality package level of services is a “taxable supply” of accommodation in a “commercial dwelling”.

Decision | Whakatau

7. The Tax Counsel Office (TCO) decided that the supply of accommodation in a serviced apartment in the village with a hospitality package provided under an ORA is a “taxable supply” of accommodation in a “commercial dwelling” as those terms are defined in s 2(1).

Reasons for decisions | Pūnga o ngā whakatau

Issue | Take: Taxable supply of accommodation in a commercial dwelling

8. The supply of accommodation in any dwelling by way of a licence to occupy will be an exempt supply under s 14 rather than a taxable supply. The supply of accommodation in a “commercial dwelling” is a taxable supply.
9. In reaching this decision, TCO first considered the meaning of “dwelling”.

Meaning of “dwelling”

10. Paragraph (b)(ii) of the definition of “dwelling” includes a residential unit in a retirement village or rest home when the consideration paid or payable for the supply of accommodation in the unit is for the right to occupy the unit.
11. If the para (b)(iii) meaning of “dwelling” applies, the units will be dwellings and will not be commercial dwellings (para (b)(ii) of the definition of “commercial dwelling”).
12. The key point in para (b)(iii) is that the consideration paid or payable for the supply of accommodation in the dwelling must be for the right to occupy the unit. If part of the consideration paid or payable is for other services, para (b)(iii) will only apply if those services are ancillary or incidental to the supply of accommodation.
13. The Commissioner considered the nature of supplies made by retirement villages in **IS 15/02: Goods and Services Tax – GST and retirement villages** *Tax Information Bulletin* Vol 27, No 11 (December 2015). The Commissioner concluded that:
 - taxpayers must identify the consideration that residents are contractually obliged to pay under the terms of the agreement;
 - if an element is merely ancillary or incidental to another element, there will be only one supply;
 - transport and emergency response services are ancillary or incidental to the supply of accommodation;
 - care services do not facilitate, enable or contribute to the supply of accommodation and are not an ancillary or incidental feature of the transaction; and
 - if a resident is required to purchase a care package, the unit forms part of a commercial dwelling.
14. The hospitality package that forms part of the ORA includes:
 - a pre-entry comprehensive health assessment by a health professional;
 - a monthly resident health check by a health professional;
 - morning and afternoon teas;
 - a weekly “high tea” event;
 - organised activities;
 - 24-hour emergency call monitoring and response;
 - access to electric vehicles;
 - recreational equipment;
 - village transport;
 - daily rubbish removal; and
 - weekly apartment cleaning.
15. The hospitality package, considered as a whole, has services that assist residents with their daily living needs. In addition, the hospitality package has a health/nursing component by including a pre-entry comprehensive health assessment and monthly health checks along with the 24-hour emergency call monitoring. TCO took the view that these care services do not facilitate, enable or contribute to the supply of accommodation and are not an ancillary or incidental feature of the transaction.
16. TCO considered that the residents receive both the supply of accommodation and care services. It follows that para (b)(iii) would not apply because the consideration paid or payable would not be solely for the supply of accommodation.
17. As para (b)(iii) does not apply, the supply is not an exempt supply of accommodation in a dwelling and will be a taxable supply.

Meaning of “commercial dwelling”

18. In para (a) of the definition of “commercial dwelling”, subparas (iii) and (v) include a convalescent home, nursing home, rest home, or hospice or premises of a similar kind to those referred in subparas (i) to (iv).
19. TCO considered whether the serviced apartments are part of a rest home and so are a “commercial dwelling” under para (a)(iii). It concluded that the level and nature of care ordinarily provided in a rest home is designed to meet much more of a resident’s needs than will be provided in the retirement village. The serviced apartments are not a rest home and do not satisfy para (a)(iii) of the definition of “commercial dwelling”.
20. TCO then considered whether the serviced apartments are “of a similar kind” to a rest home or nursing home.
21. The definition of “commercial dwelling” was considered by the Taxation Review Authority¹ where the Authority held that the approach when classifying premises that are similar to the premises listed in paragraph (a)(i) to (iv) was to:
 - begin by comparing them with their closest parallel, taking account of what that term commonly connotes at common law; and
 - then consider, to the extent necessary, the other categories of accommodation stated in the definition of commercial dwelling.
22. The closest comparable to the serviced apartments is a rest home. The ordinary meaning of “rest home” is a place where care and accommodation on a long-term or permanent basis are provided to old or frail people.
23. In the context of premises similar to a “rest home” the key is that the premises provide care services.
24. Generally, care services are in the nature of medical/nursing services and assistance with daily living. The serviced apartments provide accommodation together with some care services to assist residents. The minimum age for entry into the serviced apartments is 65. TCO considered that the care services are broadly similar to a rest home and that they are a “commercial dwelling” under para (a)(v) of its definition.

Taxable supply

25. The supply of accommodation in a commercial dwelling is a taxable supply under s 8. Therefore, having concluded that the provision of the serviced apartments with the hospitality package is the supply of accommodation in a commercial dwelling, TCO decided that the supply is a taxable supply under s 8.

1 Case L75 (1989) 11 NZTC 1,435.

TECHNICAL DECISION SUMMARIES

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TDS 25/25: Restructure and transfer of shares

Decision date | Rā o te Whakatau: 18 July 2025

Issue date | Rā Tuku: 24 October 2025

Subjects | Kaupapa

This item summarises a private ruling about the transfer of shares between companies within a group as part of a restructure and whether any future sale of the shares is taxable.

Taxation laws | Ture tāke

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

Summary of facts | Whakarāpopoto o Meka

1. The Arrangement in this ruling involves the restructure of a group company to address issues with the current structure.
2. As part of the restructure plan, investment activities, such as minority shareholdings in companies, are transferred to other entities within the group. The Applicants stated this approach is administratively easier and a more efficient option for the restructure, involving fewer banking obligations and lower compliance costs.
3. To implement this plan, shares in a company (Company A) that the parent company holds as an investment (the Shares), along with the parent company’s other investments, are sold to a wholly owned subsidiary.
4. Prior to the restructure, the possibility of the sale of Company A was signalled due to liquidity issues experienced by that company. However, a sale is not certain and there has been no commitment to sell. Whether or not Company A will be sold will depend on various factors outside of the group’s control.

Issue | Take

5. The issue considered in this ruling was whether any future sale of the Shares held by the subsidiary would be taxable under s CB 4.

Decisions | Whakatau

6. The Tax Counsel Office (TCO) concluded that s CB 4 would not apply to any future sale of the Shares held by the subsidiary on the condition that the subsidiary’s dominant purpose in acquiring the Shares must be a purpose other than to dispose of the Shares in the future.

Reasons for decisions | Pūnga o ngā whakatau

Issue | Take: Section CB 4

7. Section CB 4 provides that an amount a person derives from disposing of personal property is income of the person if they acquired it for the purposes of disposing of it.
8. The term “personal property” is defined in s YA 1 for the purposes of s CB 4 as not including land. Because shares are not land, they are “personal property” for the purposes of s CB 4.
9. Case law has developed the following principles for determining the purpose of disposal in s CB 4:¹
 - The test to determine the purpose of disposal in s CB 4 is subjective, which requires consideration of the state of mind of the taxpayer at the time of acquisition.
 - Where there is more than one purpose, taxability turns on whether the dominant purpose was to sell the personal property or other disposition.
 - Where it is necessary to establish the subjective purpose(s) of a taxpayer, the statements of the taxpayer (or of someone on their behalf) are important evidence but must be assessed and tested in the totality of circumstances. These include the circumstances of the purchase, the number of similar transactions and the circumstances of the use and disposal of the property.
 - Actions speak louder than words and the totality of circumstances may negate the taxpayer’s asserted purpose of the acquisition.
 - The mere fact that at the time of acquisition, the taxpayer contemplated the possibility of sale does not amount to a dominant purpose of sale.
10. Based on the information provided, TCO considered there are factors that suggest the subsidiary’s dominant purpose of acquiring the Shares is for the benefit of the group structure, rather than to sell. These factors include:
 - It was asserted on behalf of the subsidiary that the dominant purpose of acquiring the Shares is to implement the restructure plan for the benefit of the group structure. The documentation on the restructure plans confirmed this assertion.
 - The Shares are sold to the subsidiary along with other investments of the parent company as part of implementing a wider restructure plan to address issues with the current structure.
 - The parent company chose to transfer the Shares to the subsidiary as it was considered the most efficient and cost-effective option for the restructure.
 - A future sale of the Shares, while contemplated, is not certain and depends on various external factors. The courts have said that a mere contemplation of the possibility of sale at the time of acquisition does not amount to a dominant purpose of sale.
11. However, as mentioned at [9], the test to determine “purpose” at the time of acquisition requires the assessment of the totality of the circumstances, including the circumstances of the acquisition and the sale of the property. Further, actions may speak louder than words such that the totality of circumstances (including the actions of the taxpayer) may negate the taxpayer’s asserted purpose of the acquisition.
12. Given that the sale of the Shares is a future event and the totality of the circumstances is unknown, the ruling that s CB 4 would not apply to any future sale of the Shares was made with the condition that the subsidiary’s dominant purpose in acquiring the Shares must be a purpose other than the disposal of the Shares in the future.

¹ *CIR v National Distributors Ltd* (1989) 11 NZTC 6,346 (CA).

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 25/26: How does the business continuity test apply to a consolidated group?

Decision date | Rā o te Whakatau: 27 June 2025

Issue date | Rā Tuku: 28 October 2025

Subjects | Kaupapa

This item summarises a private ruling about the exit of two company subsidiaries from a consolidated group and the sale of a third subsidiary (the sole remaining member of the consolidated group) to a third party. It considers the business continuity test and whether a specific anti-avoidance provision applies.

Taxation laws | Ture tāke

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

Summary of facts | Whakarāpopoto o meka

1. The Applicant was a Consolidated Group of companies made up of three subsidiaries (referred to as Sub 1, Sub 2 and Sub 3) of a Parent Company.
2. The Consolidated Group had losses to carry forward. At the end of a previous income year:
 - Sub 1 and Sub 2 were in a net taxable income position; and
 - Sub 3 had incurred significant losses as part of its business activities.
3. The Parent Company intended to retain Sub 1 and Sub 2 but sell its 100% interest in Sub 3 to a third party.
4. The following steps would occur under the Arrangement:
 - Sub 1 and Sub 2 would exit from the Consolidated Group by providing the Commissioner with an election notice.
 - Sub 3 would:
 - not leave the Consolidated Group under s FM 37; and
 - continue to satisfy the eligibility criteria set out in s FM 31.
 - Sub 3 would remain as the nominated company and sole member of the Consolidated Group.
 - The Parent Company would sell its 100% interest in Sub 3 to a third party.

Issues | Take

5. The Tax Counsel Office (TCO) considered these issues:
 - Where Sub 3 was the sole remaining member of the Consolidated Group prior to an ownership continuity breach of Sub 3, whether Sub 3 was able to apply s IB 3 to carry forward losses of the Consolidated Group and whether it was the nature of Sub 3’s business which was to be considered.
 - Whether the business activities of the other entities which exited the Consolidated Group prior to the ownership continuity breach of Sub 3 were relevant when considering the requirements under s IB 3.

- Where other entities exited the Consolidated Group within 2 years prior to the ownership continuity breach of Sub 3, whether s GB 3BA would apply.

Decisions | Whakatau

6. TCO made the following decisions:

- The Consolidated Group was treated as the company that had a tax loss component arising in an earlier income year under s IB 3.
- In determining whether a major change in the nature of the business activities carried on by the Consolidated Group had occurred under s IB 3, the business activities of the Consolidated Group comprised the business activities of Sub 3.
- The business activities of Sub 1 and Sub 2 were not relevant when determining if a major change had occurred to the Consolidated Group under s IB 3.
- Section GB 3BA did not apply to the Arrangement.

Reasons for decisions | Pūnga o ngā whakatau

Issue 1 | Take tuatahi: Change of membership in a consolidated group and effect on applying the business continuity test

7. TCO considered this issue under the following headings:

- Treatment of tax losses by consolidated groups;
- Changes in Consolidated Group membership;
- Sale of Sub 3; and
- Loss carry forward.

Treatment of tax losses by consolidated groups

8. TCO analysed the treatment of tax losses by consolidated groups as follows:

- In essence, consolidation treats a group of companies owned by the same shareholders as one economic entity. Unless a provision of the Act expressly provides otherwise or the context requires another result, the Act applies to companies that are part of a consolidated group as if they were a single company (s FM 2).
- Section ID 1(1) provides that a consolidated group is treated as if it is a single company for loss purposes. The tax loss is the consolidated group's tax loss and not the tax loss of the member company.
- Sections FM 6(1)(b) and ID 1(1) are support for the position that any tax losses incurred by Sub 1, Sub 2 or Sub 3 while they were members of the Consolidated Group were deemed to be the tax losses of the Consolidated Group and not of the individual entity that incurred the tax loss.

Changes in Consolidated Group membership

- The Applicant advised that Sub 1 and Sub 2 would elect to leave the Consolidated Group. The effect was that the Consolidated Group would have one remaining member, Sub 3. Section FM 33 specifically provides that a consolidated group continues to exist if the number of group companies is reduced to one company, but if the consolidated group has no company at any time, the consolidated group no longer exists.
- TCO considered the effect of ss FM 33 and ID 1 was that the tax losses remained the Consolidated Group's tax losses and were not forfeited following the departure of Sub 1 and Sub 2 from the Consolidated Group.
- Therefore, based on the description of the Arrangement, TCO concluded that Sub 3 would remain as the nominated company and sole member of the Consolidated Group.

Sale of Sub 3

12. TCO analysed whether the Parent Company's sale of its interest in Sub 3 triggered deconsolidation of the Consolidated Group, as follows:
 - If a company that was a member of a consolidated group was sold and was no longer in the same wholly owned group of companies as the other members, it would no longer be eligible to be a member of the consolidated group (s FM 31(1)(eb)). However, the sale of shares in a company did not in itself result in that company losing its eligibility to be a member of a consolidated group.
 - If the consolidated group had only one member, the sale of the shares in the member did not result in the member leaving the consolidated group. That is, the consolidated group would continue under the new ownership.
13. It followed that the Consolidated Group would not be deconsolidated and would continue to exist after:
 - Sub 1 and Sub 2 chose to leave the consolidated Group; and
 - the Parent Company sold its interest in Sub 3.

Loss carry forward

14. As the Consolidated Group would continue to exist after the Parent Company sold Sub 3, the next step for TCO was to determine whether any of the Consolidated Group's tax losses could be carried forward and used in future tax years.

Ownership continuity test

15. TCO considered:
 - a company could carry forward a loss balance if there had been at least 49% ownership continuity for the continuity period (s IA 5); and
 - the Parent Company's sale of Sub 3 would result in a breach in the ownership continuity test. The Consolidated Group's tax losses would be forfeited unless the business continuity test could be satisfied.

Business continuity test

16. In cases where the ownership continuity test was breached, a company would still be able to carry forward its tax losses if the business continuity test (BCT) in s IB 3 was satisfied.
17. One requirement of the BCT is there has been no major change in the nature of the business activities carried on by the company during the business continuity period, unless the change was a permitted major change (s IB 3(2)(c) and s IB 3(5)).
18. Even if s IB 3 applied, TCO noted that targeted anti-avoidance rules in ss GB 3BAB and GB 3BAC might apply to negate any benefit of s IB 3.
19. TCO was asked to rule on how the BCT would apply in the context of a consolidated group's business activities.

Applying the BCT to a consolidated group

20. As stated at [8], TCO considered a consolidated group was treated as a single company. That is, the tax loss provisions in Part I of the Act would apply with modifications to a consolidated group as if it were one tax entity.
21. Therefore, before Sub 1 and Sub 2 left the Consolidated Group, the Consolidated Group's business activities consisted of the three Subs' businesses. However, after Sub 1 and Sub 2 elected to leave the Consolidated Group, the Consolidated Group's business activity would consist solely of Sub 3's business.
22. In determining whether the BCT could apply to the Consolidated Group following an ownership continuity breach, TCO considered the key issue was what the business continuity period was.

Business continuity period

23. Section IB 4 defines "business continuity period".
24. TCO considered the business continuity period would start immediately before the ownership continuity breach, rather than on the date that the tax loss was incurred. Therefore, if Sub 1 and Sub 2 were not members of the Consolidated Group, and Sub 3 was the sole member immediately before an ownership continuity breach occurred, then for the purpose of determining if the business continuity test applied, the business activity to consider was Sub 3's, and not the business activity of Sub 1 or Sub 2.

25. TCO reached the following conclusions:

- The Consolidated Group was treated as the company that has a tax loss component arising in an earlier income year under s IB 3.
- In determining whether a major change in the nature of the business activities of the Consolidated Group had occurred under s IB 3, the business activities of the Consolidated Group were considered to be comprised of the business activities of Sub 3.
- The business activities of Sub 1 and Sub 2 were not relevant when determining if a major change has occurred to the Consolidated Group under s IB 3.

Issue 2 | Take tuarua: Anti-avoidance

26. This second issue was to establish, where other entities exited the Consolidated Group within 2 years before the ownership continuity breach of Sub 3, whether s GB 3BA would apply.
27. TCO considered s GB 3BA was a specific anti-avoidance rule that may apply when a company carries a tax loss forward under the BCT. Section GB 3BA has the following requirements:
- A share in a company known as the “loss company” or a share in another company was subject to an arrangement.
 - The arrangement was entered into within the 2 years immediately preceding a breach of the continuity of ownership requirements in s IA 5.
 - The arrangement allowed the loss company to meet the requirements of s IB 3(2).
 - A purpose of the arrangement was to defeat the intent and application of s IB 3.

Purpose of the arrangement was to defeat the intent and application of s IB 3

28. TCO focused on s GB 3BA(1)(d). Section GB 3BA(1)(d) requires that a purpose of the arrangement was to defeat the intent and application of s IB 3. It was not necessary for the purpose to be the dominant or main purpose of the arrangement. It was sufficient if a purpose of the arrangement was to defeat the intent and application of s IB 3.
29. TCO considered that the same principles that applied to s BG 1 (general anti-avoidance rule) would apply to s GB 3BA. This meant that if the effect of an arrangement, determined objectively, was to defeat the intent and application of s IB 3, that will be the purpose of the arrangement.
30. The Supreme Court in *Ben Nevis* considered it desirable to settle the approach to applying s BG 1.¹ This approach is referred to as the Parliamentary contemplation test, which is an intensely fact-based inquiry. *Ben Nevis* has been followed in subsequent judicial decisions.
31. TCO's approach in making this decision was consistent with *Tax avoidance and the interpretation of the general anti-avoidance provisions sections BG 1 and GA 1 of the Income Tax Act 2007* (3 February 2023) (IS 23/01). IS 23/01 will not be replicated in this TDS but in summary the steps are as follows:
- Understanding the legal form of the arrangement. This involves identifying and understanding the steps and transactions that make up the arrangement, the commercial or private purposes of the arrangement and the arrangement's tax effects.
 - Determining whether the arrangement has a tax avoidance purpose or effect. This involves:
 - Identifying and understanding Parliament's purpose for the specific provisions that are used or circumvented by the arrangement.
 - Understanding the commercial and economic reality of the arrangement as a whole by using the factors identified by the courts. Artificiality and contrivance are significant factors.
 - Considering the implications of the preceding steps and answering the ultimate question under the Parliamentary contemplation test: Does the arrangement, when viewed in a commercially and economically realistic way, make use of or circumvent the specific provisions in a manner consistent with Parliament's purpose?
 - If the arrangement has a tax avoidance purpose or effect that is not the sole purpose or effect of the arrangement, consider the merely incidental test. The merely incidental test considers many of the same matters that are considered under the Parliamentary contemplation test.

¹ *Ben Nevis Forestry Ventures Ltd v CIR* [2008] NZSC 115, [2009] 2 NZLR 289.

32. Taking into account all of the relevant facts and circumstances (noting that as this is a summary it may not contain all the facts or assumptions relevant to the decision and, therefore, cannot be relied on) the TCO concluded as follows.

Purpose of s IB 3

33. Section IB 3 allows a loss company that has breached the ownership continuity threshold to carry its loss balance forward if no major change has occurred in the nature of the business activities the company carries on during the applicable business continuity period (other than a permitted major change). Parliament's specific purpose for s IB 3 is to allow a company to carry a loss balance forward despite a continuity of ownership breach if the business the company carries on before the breach is the same business that the company carries on after the breach.
34. The specific purpose of the BCT rules is contained in s IB 1. Section IB 1 is a clear legislative statement of Parliament's purpose for s IB 3. Namely:
- a loss will be carried forward under s IB 3 only if the business a loss company carries on before a breach of ownership continuity is in commercial and economic reality the same as the business it carries on after the breach; and
 - a loss will not be carried forward under s IB 3 as part of a loss trading transaction.

The arrangement's purpose is not inconsistent with the purpose of s IB 3

35. As [13] describes, the Arrangement has two steps:
- Sub 1 and Sub 2 elected to leave the Consolidated Group; and
 - the Parent Company sold its shares in Sub 3.
36. While the Arrangement has resulted in a change in the Consolidated Group's business activities, TCO considered that the Arrangement was not inconsistent with Parliament's purpose for s IB 3:
- The Parent Company's proposed sale of Sub 3 would be the sale of a genuine commercial business. Sub 3 had significant assets and the current phase in its business lifecycle meant that it had commercial value in addition to any potential future tax savings represented by the Consolidated Group's carried forward loss balance.
 - There was a commercial reason for removing Sub 1 and Sub 2 from the Consolidated Group because purchasers would have no interest in buying those companies as part of the Consolidated Group. This step was not artificial or contrived. It was not there to allow the Consolidated Group to meet the requirements of s IB 3.
 - The benefit of the Consolidated Group's tax losses would remain with the business activities (Sub 3's business) that incurred the tax losses.
 - The Arrangement was not a loss trading transaction. Loss trading occurred where there was little or no economic basis for the transaction in which a company was acquired. Its principal purpose was the purchase of losses that would otherwise not be used. There was a clear commercial or economic basis for the sale of Sub 3, an established business. Further, in the absence of any evidence to the contrary, it appeared that the Consolidated Group's tax losses would be used in the future if the Arrangement did not occur. This was not the case of a taxpayer that was in the process of winding down and only had value due to its tax loss profile.
37. In summary, TCO considered the Arrangement was not inconsistent with the purpose and intent of the BCT and that s GB 3BA did not apply to the Arrangement. On this basis, TCO did not need to conclude on the other requirements of s GB 3BA.

REGULAR CONTRIBUTORS TO THE TIB

Tax Counsel Office

The Tax Counsel Office (TCO) 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 TCO 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 Services

Legal Services 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.

Technical Standards

Technical Standards sits within Legal Services and contributes 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. Technical Standards also contributes to the "Your opportunity to comment" section.

Policy

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.