NEW ZEALAND LAW SOCIETY
NZLS EST 1869

149 Taranaki Street, Wellington
DX SP20202, Wellington
PO Box 5041, Wellington 6140, New Zealand

TEL 04 472 7837 · E inquiries@lawsociety.org.nz
www.lawsociety.org.nz

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Public Consultation
Inland Revenue
Wellington

By email: public.consultation@ird.govt.nz

RE: Draft Interpretation Statement: Income Tax – When is development or division work "minor"?

1. The New Zealand Law Society's Tax Law Committee welcomes the opportunity to comment on draft Interpretation Statement: *Income tax – when is development or division work minor?* (draft IS).

2. The draft IS sets out the Commissioner's guidance on section CB 12(1) of the Income Tax Act 2007. The stated scope of the draft IS is to provide guidance to taxpayers on when development or division work is minor. However, the draft IS also includes detailed commentary on the statutory components of section CB 12(1).

When does an undertaking or scheme involve the development of the land or the division of the land into lots?

3. In respect of section CB 12(1), the draft IS considers paragraph (a) - what constitutes a "scheme or undertaking" (paragraphs 34 to 42 of the draft IS) and paragraph (c) - what is carrying on a development or division work relating to land (paragraphs 43 to 72 of the draft IS). The draft IS does not, however, consider paragraph (b) - when "the undertaking or scheme involves the development of the land or the division of the land into lots".

4. It would be useful for the draft IS to separately consider the meaning of paragraph (b) of section CB 12(1). In our view, section CB 12(1) should be interpreted as a composite phrase, as not all undertakings or schemes which involve development or division work necessarily involve the development of the land or the division of land into lots, which is what section CB 12(1) is directed at. We suggest that the draft IS considers each of three statutory components of CB 12(1) (being CB 12(1)(a), CB 12(1)(b) and CB 12(1)(c)). This proper statutory construction should also be reflected in other places in the draft IS, such as paragraph 13.

5. We consider that a scheme to rezone land or to obtain a resource consent to develop or subdivide land, but where the scheme does not include completing any actual development or division, does not constitute an undertaking or scheme which involves the development of the land or the division of the land into lots. This is consistent with the Commissioner's conclusions on what constitutes a scheme involving the division of land into lots (by reference to *Wellington v C of IR* (1981) 5 NZTC 61,101, and the High Court and TRA cases that cite it) in paragraphs 47 and 48 of the draft IS (where the Commissioner states that a

scheme for division includes the completion of the subdivision by the deposit of plans and issue of titles).

6. A scheme which is confined to a zoning change or obtaining a resource consent for subdivision may still be subject to income tax under section CB 14(1) of the Income Tax Act 2007 if the requirements of that section are satisfied (including that the land is sold within 10 years of the date it is acquired). On this basis, if the only activity is applying for a resource consent, subdivision consent or a specified departure to an operative District Plan (i.e. applying for the land to be rezoned), there is not an undertaking or scheme involving the development of land or division into lots which could be subject to section CB 12(1).

7. In some dealings with Inland Revenue, *Church v C of IR* (1992) 14 NZTC 9,196 has been cited as authority for the proposition that a scheme contemplated by the taxpayer, but which falls short of the actual development of the land or the actual division of the land into lots, is nevertheless a scheme caught by sections CB 12 and CB 13. While *Church* is relevant where a scheme that falls within the ambit of sections CB 12 or CB 13 has been abandoned, *Church* is not relevant where the scheme contemplated by the taxpayer falls short of a scheme to which sections CB 12 or CB 13 apply.

Changing an undertaking or scheme

8. It would be helpful if the draft IS included comment on how section CB 12(1) applies where a development starts and is abandoned, and subsequently a different (or the same) development scheme arises. In other words, how does section CB 12(1) apply where development work occurs, and a development scheme arises separately but in relation to the same land?

Boundary adjustments, amalgamations, cross-leases and unit titling

9. The draft IS considers whether a boundary adjustment constitutes a scheme involving the division of land into lots. The draft IS should confirm that a scheme or undertaking involving the amalgamation of titles (e.g. *Case R7* (1994) 16 NZTC 6,035), a cross-lease and unit titling (e.g. *Costello v C of IR* (1993) 15 NZTC 10,285) are also division schemes. It would also be helpful for the Commissioner to advise her view whether an amalgamation of two lots into one involves the division of land into lots (as the end result is the creation of a single lot).

Absolute value

10. Ascertaining whether work is minor is a question of fact and degree having regard to a range of various factors. However, in paragraph 91 of the draft IS, the Commissioner considers that a point will be reached where the absolute value of the sum spent on the development or division is so high that the work is more than minor.

11. If this is the case, then the Commissioner should advise taxpayers what that figure is. To that end, we note that:

    a. Example 1 concerns a scheme involving $15,000 of costs, which was considered to be minor;

    b. Example 2 concerns a scheme involving $50,000 of costs, which was considered to be “significant in absolute terms (when compared with development and division work in case law)”, although other factors were also relevant in that example;

c. Example 3 concerns a scheme involving $18,500 of costs, which the Commissioner regarded as "low";

d. Example 4 concerns a scheme involving $5,000 of costs, which the Commissioner concluded "was not significant compared with the value of the land"; and

e. Table 1 refers to *Case P61* (1992) 14 NZTC 4,416, where the sum of $18,460 (in 2019-dollar terms) expended on a division scheme was considered to be minor.

12. In the light of the above, we infer that the Commissioner's "bright-line" in terms of absolute costs could be in excess of $15,000 and is perhaps less than $50,000, but more precision would be welcomed. The examples refer to multiple factors, so it is difficult to gauge the Commissioner's view on what absolute value alone would give rise to a "more than minor" development or division.

Removal of example 3 of IG0010

13. The draft IS replaces an earlier interpretation guideline, IG0010, "Work of a minor nature" (February, 2005) (IG0010). Example 3 of IG0010 has been removed from the draft IS and replaced with a different example.

14. Example 3 of IG0010 provided much needed clarity to taxpayers and their advisors because the Commissioner considered this example to be a borderline case where work was still of a minor nature. It would be helpful if an updated version of Example 3 of IG0010 was included in the draft IS.

Style and minor errors

15. We point out below aspects of the draft which would benefit from re-drafting:

a. The land gain taxation provisions in paragraph 15 have been misdescribed (e.g. section CB 6), and should also include section CB 15(1) (which is not an independent charging provision).

b. The last two bullet points in paragraph 17 are imprecise and could be expressed more clearly.

c. Footnotes 2 and 4 incorrectly refer to the Income Tax Act 1976 as the Income Tax Act 1974.

d. Cooke J's name is misspelt in paragraph 20.

e. The reference to section CB 15 at the beginning of paragraph 27 should be to section CB 15(1).

16. We trust Inland Revenue will find these comments helpful. If you wish to discuss these comments, please do not hesitate to contact the Tax Law Committee convenor Neil Russ, through the Law Society's Law Reform Adviser, Emily Sutton (Emily.Sutton@lawsociety.org.nz).

Yours faithfully

Herman Visagie
Vice President