

Victoria University of Wellington Tax Working Group
CONFERENCE: A TAX SYSTEM FOR NEW ZEALAND'S FUTURE

1 December 2009 Afternoon Session 1

Base broadening – taxation of capital income

Discussant: Professor John Prebble, Victoria University of Wellington

THE CAPITAL/REVENUE DISTINCTION IN PRACTICE

1. Introduction

Topic of session: base broadening
Capital/revenue distinction
John Shewan and Gareth Morgan: economic perspective

2. My focus

Difficulty of applying the capital/revenue distinction in practice
Start with NZ's simplest statutory rule:
Buy something with the intention of selling it
Pay tax on the profit on sale

3. Example: a dairy farmer

Sells milk
Sells the farm, owned 40 years
Buys abandoned dairy factory
Promotes company to make fashionable cheese
Sells factory to the company

4. Inconsistent United Kingdom cases

Rutledge v Inland Revenue Commissioners, Court of Appeal, 1929
Jones v Leeming, Court of Appeal, affirmed House of Lords, 1930

5. Income Tax Act 2007 section CB 6(1)(a)

Sale of land
Acquired for one or more purposes
That included the purpose of disposing of the land

6. Anzamco Ltd (in liq) v CIR (1983) Barker J, High Court

Anzamco: private company of
Mormon missionaries from Utah
Leader: Wendell S Mendenhall
They wanted a New Zealand holiday home

7. 1966 Anzamco bought

20,000 acres of Tuhoe land on Napier Taupo Road
Developed land as a ranch
El Rancho Poronui

8. El Rancho funding

Funds from USA
Permission of Minister of Finance to import money

9. Condition of permission

Promise to subdivide and sell half of El Rancho to NZ farmers
Wendell signed a deed
Formal covenant to confirm Anzamco's promise

10. Sale 1980

Missionaries retired or died
Anzamco sold El Rancho in one lot

11. Commissioner assessed half the profit under predecessor to section CB 6(1)(a)

He said:
Anzamco bought half the land with purpose of sale
Evidence: deed promising sale
“Wendell was economical as to his intentions”

12. CIR v Boanas, the Mount Rosa case (2008) High Court Dobson J

Taxpayers in 1993
Bought pastoral lease of Mt Rosa Station
May 1997: acquired freehold title from the Crown
“Within months” embarked on initiatives for subdivision and vineyard

13. Sale of Mount Rosa

February 2000 sold land to taxpayers’ company
2000: planted 6 hectares of grapes, more since

14. Issue

Did taxpayers intend to sell at May 1997?
Commissioner decided, “yes”
Therefore taxed the profit

15. CIR: evidence of purpose of disposal at acquisition in 1997:

1996 taxpayers obtained tax advice about subdivision
Speed of the sale
Lots of other evidence
All explained: advice for neighbour: no intent of sale in May 1997
Judge Barber agreed; Justice Dobson upheld him on appeal

16. Income Tax Act 2007 section CB 12(1)(b) & (e)

Land sold after scheme
Involving the development of the land
Or involving the division of the land into lots
Scheme started within 10 years of acquisition

17. Anzamco assessed also under predecessor to section CB 12(1)(b) & (e)

Ranch development started within 10 years of acquisition
Profit taxable
No matter that development was farm development

18. Apply to Mount Rosa? Facts:

Acquisition 1993 and 1997
Website says 6 hectares planted in 2000
That is, development scheme started within 10 years of acquisition

19. Tax position

Commissioner did not invoke section CB 12
Perhaps CD 12 eliminated at procedural stages?
CB 12 issue: did development scheme begin before February 2000?
Were there before then:
Irrigation? Farm tracks? Fences?