# Commercial law 301 Taxation Cases and Principles

What is Income?/ The Nature of Income/CA 1(1), CA 1 (2)

1. INCOME IS 'SOMETHING THAT COMES IN':

***Tennant v Simth 1892:*** realisation rather than an imputed gain. If a benefit saves a person from expenditure that is not income, **the saving is not income because it does not come in**.

Imputed Income= **Imputed income** is the accession to wealth that can be attributed, or imputed, to a person when they avoid paying for services by providing the services to themselves, or when the person avoids paying rent for durable goods by owning the durable goods, as in the case of imputed rent

***FCT v Cook and Sherden:*** Soft drink retailers received a free holiday from the manufacturer- non convertible in to money or money's worth = Not Income

***FCT v Payne:*** Air miles under frequent flyer scheme = Not Income

2. INCOME IS 'MONEY OR MONEY'S WORTH':

***Dawson v CIR:*** TP held debenture stock and received a TV for 5 years. Held: the benefit was not income as not in monetary form and not convertible into money. SEE CC7

3. INCOME IS FROM PROPERTY OR LABOUR:

***Brent v FCT:*** TP sold her story to the Newspaper- out of a sum total of $65,250 she only received $10,000 during the relevant income year. High court of AU: Income, she was only assessable in that income year

4. INCOME HAS A CERTAIN QUALITY IN THE HANDS OF THE RECIPIENT:

***Scott v FCT:*** TP was a solicitor engaged in the administration of the estate of a deceased client – the client's widow gave the TP $10,000. HELD: It was a gift, not assessable income.

***G v CIR:*** TP was an evangelist preacher and got donations for several years from donors in rural north island- he supported himself out of the donations. HELD: some of the donations, not all, were taxable income receipts, not gifts, as he relied upon them for his support and expected to receive them.

5. INCOME HAS; PERIODICITY, RECURRANCE, AND REGULARITY:

***FCT v Dixon:*** Weekly payments from his former employer to make up the difference between his civil military pay. Held: Income

***Reid v CIR***: Trainee teacher received a student allowance. Held: income was a regular periodic payment made to defray his expenses while at teacher's training college.

***FCT v Harris:*** Retired former employee received 4 ex gratia payments from his previous employer to supplement his pension. First payment was assessed to Income Tax by Commissioner. Held: First was not income. (Other 3 however were).

6. ILLEGAL ACTIVITIES

(Income from illegal businesses or activities will still be caught and subject to tax.)

***Lindsay v IRC:*** Whiskey transport during Prohibition in U.S. Held: assessable income.

## What is not income?

CAPITAL: ***((e)= capital expenditure (r)=capital receipt)***

***Eisner v Macomber:*** "The fundamental relation of 'capital' to 'income' has been much discussed by economists, the former being likened to the **tree** on the land, the latter to the **fruit or the crop"**

(Income earning structure vs Income earning process)

What is on capital account?

****(e)Sun Newspapers v FCT:*** SN bought out competitor 'The World' owner's share, to stop them publishing another newspaper in the area. Soon after 'The World' ceased publication. SN tried to claim that the expenditure was an expense and therefore deductible. Held: the Expenditure added was on capital account, as it enlarged the goodwill of the business. = Non-deductible

****(e)BP Australia v FC of T:*** BP paid service stations money in order to obtain trade tie in agreements which meant that the services could only sell BP products over the next 5 years. BP tried to deduct this. FC of T said it was on capital account. Privy Council suggested the following should be considered.

- Need or occasion which calls for the expenditure
- Fixed or circulating capital (turnover)?
- Payments of a **once and for all nature**, producing assets or advantages of an enduring benefit?
- Length of time of the tie agreements
- Treatment on ordinary principles of commercial accounting
- Does it relate to the Business structure or Money earning process?

And:

- The way in which the desired benefit was to be used
- One off or a recurring nature

Held: The tie in agreements were part of the ordinary process of selling the TP's products. The payments were periodic. = Revenue account, deductible.

***Their lordships stated in this case that there is no specific test, and each case must be based on their individual facts***

***(e)Auckland Gas Co Ltd v C of IR:*** Insertion of a polyethylene pipe into its old cast iron network instead of replacing the original. Held: This was more than just repair and maintenance, this was upgrade. = non-deductible, on capital account. (Major principles of BP Australia were reiterated in this NZ case)

Recurring payments:

On capital account:

***(e)Christchurch Press Co Ltd v C of IR:*** Employed electricians and engineers to maintain and service **printing presses** used in the production of newspapers (main business). over a seven week period C.P.C ltd paid the electricians to wire up an extension to the printing press. C.P.C ltd tried to deduct this as expense. Held: The work was related to the acquisition of a capital asset.

On revenue account:

***(e)Goodman Fielder Wattie Ltd v FC of T:*** Wages paid to researchers employed by a **pharmaceutical company**. Held: R&D was the primary business activity of the company.

One off Payments:

***(Once and for all test)***

***Vallambrosa Rubber Co Ltd v Farmer (surveyor of taxes):*** not "final or determinative", "it is not a bad criterion of what is capital expenditure to say that capital expenditure is a thing that is going to be once and for all, and income expenditure is a thing that is going to recur every year".

Capital account:

***(Enduring Benefit Test, Generally favoured by the courts)***

***(e)British Insulated and Helsby Cables Ltd v Atherton:*** TP claimed a deduction for **establishing a superannuation fund** for its salaried staff. Held: a payment that is once and for all, that leads to an enduring benefit is on capital account.

Revenue Account:

***(e) (not great) Hancock v General Revisionary & Investments Co:*** TP purchased an Annuity for retired Actuary. Held: Revenue Account

Capital Receipts: (see Business Income CB 1)

One off receipt:

***(r) Californian Copper Syndicate v Harris:*** TP was in business of acquiring mines particularly **copper mines**. Acquired a mine, made improvements to the mine then sold it/ traded for shares in purchaser Co. HELD: as it was in the business of selling mines etc it was income = ASESSABLE. (Caveat: had it not been in the business, and it was simply an ordinary investment it would have been capital. See page 38 CB)

Multiple Receipts:

***(r)FCT v Whitfords Beach Pty. Ltd:*** TP owned land by the **beach** which was used **for** recreational fishing activities. TP Co owned multiple plots. Land went up in value and so entered on a scheme in which to make a profit. High Court of Australia HELD: The scheme was more than a realisation of a capital asset. INCOME = ASSESABLE.

## Fixed or Circulating Capital:

See: See Californian Copper Syndicate v Harris (above)

### Circulating capital

***<u>(e)Inglis:</u>*** TP wanted to **deduct losses on shares,** commissioner said losses were on capital account and non-deductible. Court of Appeal Held: Property bought for the **<u>intention</u>** of resale takes the nature of circulating capital, (even if you would usually deem it as fixed). Revenue Account = Deductible. (see S CB 4 ITA)

## ***<u>(e) TRUSTPOWER</u>***

- **Facts:** TP is a generator & retailer of electricity - generates ½ the electricity it sells & buys in the other 1/2. TP's business income is derived from retail sales.
- During IYs 2006-8, TP took preliminary steps - applied for &obtained resource consents.
- Resource consents: land use (unlimited duration); water permits (fixed periods between 10-15 years); & discharge permits (fixed periods between 10-15 years).
- Part of TP's development pipeline that provides TP with information about feasibility & costs of building new generation capacity.
- **TP claimed** that expenditure incurred as part of feasibility analysis & before it had made its build or buy decision. TP also claimed that consents were not standalone assets separate from the projects to which they related & so were deductible as on revenue account (no apportionment sought).
- **CIR claimed**: the resource consents for water permits &discharge permits were intangible capital assets (not the unlimited land use rights as these had no fixed term so could not be expected to decline in value) & in any event all the expenditure was subject to the capital limitation.
- **<u>Issue</u>: is approximately $18 million expenditure incurred by TrustPower deductible in 2006, 2007 & 2008 tax years as revenue account property or is it capital expenditure that can be depreciated?**
- **Court of Appeal:** There is a need for an **objective analysis of the factual background** relating to the **nature & purpose or effect of the expenditure** & **not** a **subjective** approach based on views of witnesses from either side.
- The **object** of the expenditure **was capital even if** as a matter of corporate governance there had been **no final decision made** about whether to apply for resource consents.
- Did not accept argument that the value of the resource consents was tenuous at best & would not block competitors from competing in those areas.
- Rather the **resource consents gave TP valuable rights** which were **essential** to TP's long term programme of **future capital works**. Resource consents were