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Our ref 160408KPMGSubCB6

8 April 2016

Dear Sir or Madam

**KPMG Submission - PUB00260: Land acquired for a purpose or with an intention of disposal**

KPMG is pleased to make a submission on the above draft Question We've Been Asked ("QWBA") item.

**Need for greater taxpayer education**

We consider that guidance on the application of the intention test for land (section CB 6) is timely, particularly with the introduction of the new bright-line rule (section CB 6A) from 1 October 2015.

In KPMG's experience from educating taxpayers and various participants in the land transfer process on the application of the bright-line rule, there appears to be a general lack of understanding of how proceeds from the sale of land could be taxable under other rules, including section CB 6.

Therefore, to have maximum impact, we believe the finalised QWBA needs to be widely circulated to the general public. This means using communication channels beyond those employed normally for Commissioner's statements, such as Tax Information Bulletins.

For example, the QWBA content should be included in the IR 264 rental income guide, which already includes a section on the bright-line rule. The item should also receive prominent coverage on Inland Revenue's website, once published.

**Consolidating the various Inland Revenue guidance on the land sale rules**

The Commissioner should also take the opportunity to consolidate the various guidance released on the application of the land sale rules.

We note that some of the more recent guidance released by Inland Revenue on different aspects of the land sale rules includes:

- QB 15/13: Whether the cost of acquiring an option to acquire revenue account land is deductible.
- QB 15/04: Whether it is possible that the disposal of land that is part of an undertaking or scheme involving development or division will not give rise to income, even if no exclusion applies.
- QB 15/02: Major development or division – what is “significant expenditure” for section CB 13 purposes?
- Tax Information Bulletin (“TIB”) item on “Clarifying the acquisition date of land” in section CB 15B. (We note that this is not a Commissioner’s Statement, however, the TIB is an important statement of how new section CB 15B is intended to operate.)

One of the challenges for taxpayers is determining whether the Commissioner has a view on a particular aspect of the land sale rules. The current process requires a search of Inland Revenue’s website, which is not the most user-friendly, and knowledge of the appropriate terminology. Alternatively, taxpayers need to seek specialist advice at cost.

We believe that the Commissioner’s guidance should be consolidated, if not in a single document, then at least on a single page on the Department’s website to make navigation and search easier.

### **Our detailed submissions**

We broadly agree with the conclusions of the draft QWBA. Our comments are in relation to the following specific issues. We have also attached a marked-up version of the QWBA to highlight how some of our submissions below can be implemented.

#### ***Application of the residential land exclusion (section CB 16)***

Paragraph 5 of the draft QWBA outlines the two key exclusions from section CB 6, the residential land and business premises exemptions.

In relation to the former, there is little analysis on when a property that would otherwise be subject to section CB 6 would not be taxable because it qualifies as residential land. In particular, there is no discussion of what “occupied mainly as a residence” by a person and any member of their family means.

We note that uncertainty arose under the “main home” exemption, in section CB 16A, which is worded differently to the residential land exclusion. (We note that this was once of the concerns submitters, including KPMG, raised.)

For the main home exemption rule in section CB 16A to apply, the land must be (i) used predominantly as a person’s main home; and (ii) used for most of the time as their main home.

In the Special Report on the bright-line rule, Officials indicated that it (i) should be calculated by reference to the area of land used for residential and non-residential purposes and (ii) requires the property to have been used more than 50% of the time as a main home. (While the

Special Report does not carry legislative weight, at a minimum it at least clarifies the stated legislative intent of section CB 16A.)

Our concern is the Commissioner applying the interpretation in the Special Report to also determine whether land is occupied mainly as a residence, for section CB 16 purposes. It should be explicitly clarified in the QWBA that this will not be the case as these are different legislative exemptions. If Parliament had intended for the same exclusion to apply, then it would have subjected section CB 6A to section CB 16, instead of including new section CB 16A.

For optimum clarity, however, the Commissioner should outline in the QWBA what factors she will consider when determining whether section CB 16 is applicable.

### ***Definition of “land”***

Paragraph 19 notes that “land” could include any estate or interest in land (including an option). Importantly, the land sale rules will also apply to leasehold interests and equitable interests in land. However, the draft QWBA does not expand on the potential impacts of the land sales rules applying.

This appears to be an area which is often overlooked, including by the Commissioner when providing draft guidance. KPMG noted in its submission on the Taxation (Bright-line Test for Residential Land) Bill our concern with the potential application of the bright-line rule on expiry of leasehold interests. The Official’s Report response was that this would not be a disposal, for tax purposes, even though this is, to us, the logical outcome when applying the analysis in QB 15/13 on expiry of an option over land. This highlights to us the potential difficulties in interpretation in this area, and the scope to take a different view to the Commissioner.

### ***Misstatement of the application of bright-line test (and other land sale rules)***

We have concerns with how discussion of the bright-line rule has been incorporated in the draft QWBA.

The technical application (or non-application) of that rule is misstated in the main analysis and the Examples. The bright-line rule (in section CB 6A) only applies if sections CB 6 to CB 12 do not apply. Consideration therefore needs to be given to the “other” land sale rules first.

This is not necessarily the same as saying that, if the bright-line test is not applicable, the other land sale rules may apply (in paragraph 7), or that the other land sale rules (e.g. section CB 6) need not be considered if the bright-line test applies (in paragraph 28), which is technically wrong as those rules must be considered first.

We acknowledge that practically the same outcome may arise. However, stating the correct approach is important, particularly for applying the Residential Land Withholding Tax, once those rules are enacted.

Paragraph 26 states that the Examples do not consider whether any of the other land sales rules apply. In fact, the Examples do consider the application of section CB 6A.

In our mark-up, we have removed unnecessary references to section CB 6A in the QWBA to simplify the analysis and the Examples.

### ***Deductibility of costs***

Paragraph 21 of the draft QWBA states that a deduction for the cost of land, capital improvements, and other holding costs (e.g. interest, insurance, repairs and maintenance) is subject to meeting the requirements of sections DA 1, DA 2, DB 6 and DB 23.

If the gain from the sale of land is taxable under section CB 6, then the general permission (in section DA 1) should be met, and neither the capital limitation, private limitation nor any other general limitations (in section DA 2) should be applicable to limit the deductibility of costs.

This is because:

- The application of section CB 6 to the sales proceeds provides sufficient nexus with derivation of assessable income, such that the general permission is satisfied;
- The capital limitation is not applicable as the gain will be of a revenue nature (again due to the application of section CB 6 to the proceeds);
- The private limitation is not applicable as the gain will not be of a private or domestic nature (i.e. the residential land exclusion in section CB 16 will not be applicable); and
- The interest deductibility (section DB 6) and deduction for cost of revenue account property (section DB 23) provisions override the capital limitation (and as noted above, the general permission will be met).

This should be made explicit in the draft QWBA. Again, we have attempted to clarify this in our mark-up of the QWBA.

Similarly, the Examples confirm the deductibility of costs of any repairs and maintenance on the properties that are not capital in nature. We cannot see how repairs and maintenance can be capital in nature. If properly characterised as repairs, the expenditure is not capital in nature and would be deductible. If capital, then the repairs would be properly characterised as improvements. A deduction would be allowed under section DB 23. We have made some deletions to the QWBA to reflect this.

We acknowledge that this may be a drafting issue – intended to convey that the capital limitation applies to unspecified expenditure. If that is the case, this should be separated from the items which are not capital in nature.

### ***Examples in the draft QWBA***

We support the inclusion of examples in the draft QWBA. However, our concern is that they are too stylized (in particular Examples 3, 4 and 5) to generate a conclusion that is largely beyond argument.

The fact patterns of some of the Examples are too convoluted and crowded. By way of illustration, Example 3, where Taj acquires 28 properties, sells 23 of the properties and within

six months of each sale buys a new replacement property. We assume the main point of this example is to illustrate that the stated reasons for disposal do not stack up. However, this point can still be made with a much simpler fact pattern. A consequence of the fact pattern is the conclusion that all of the properties are similarly tainted. It may well be, objectively, that some properties, acquired for rental purposes were genuinely sold due to unsolicited offers to purchase and/or financial difficulties (which as noted under Example 1 is an appropriate defence against the application of section CB 6). This demonstrates the dangers of a “kitchen sink” analysis, rather than evaluating the facts and circumstances of each transaction separately.

In the case of Example 5, it is unclear what impact (if any) the marketing of the potential capital growth of an investment property would have on whether section CB 6 applies, as compared to Chris having a fixed investment horizon of 3 to 5 years for the property. It seems to us that the latter is the critical reason for the revenue account conclusion in that Example. This should be clarified in the QWBA. Most marketing materials for investment properties, particularly in the current housing market, will emphasise potential capital returns. This, in and of itself, should not be used as a proxy for intention of resale, if the property is subsequently sold.

We also consider that it is important that it is Chris (and not the marketing agent) who has an expectation of capital growth. We acknowledge that objective evidence may however be difficult to find.

Similar to concerns we have raised previously in relation to other published QWBAs and Commissioner’s Statements, the Examples are not helpful in providing guidance on the difficult boundary issues taxpayers may face. They are therefore limited in their illustrative value.

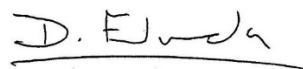
### **Further information**

Please do not hesitate to contact us, John Cantin on 04 816 4518, or Darshana Elwela on 09 367 5940, if you require further information on our submission.

Yours sincerely



John Cantin  
Partner



Darshana Elwela  
National Tax Director

EXPOSURE DRAFT - FOR COMMENT AND DISCUSSION ONLY

Deadline for comment: 7 April 2016. Please quote reference: PUB00260.

QUESTION WE'VE BEEN ASKED QB XX/XX [KPMG suggested drafting changes]

**INCOME TAX – LAND ACQUIRED FOR A PURPOSE OR WITH AN INTENTION OF DISPOSAL**

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

This Question We've Been Asked is about s CB 6.

**Question**

1. When will the proceeds of the sale of land need to be included as income for tax purposes, under s CB 6?

**Answer**

2. If you buy land for a purpose or with an intention of selling it, the proceeds of the eventual sale, whenever that occurs, will be income under s CB 6 unless one of the exclusions from that rule (for residential land and business premises) applies.

**Explanation**

**What is the relevant taxing provision?**

3. Section CB 6(1) provides that:

**CB 6 Disposal: land acquired for purpose or with intention of disposal**

*Income*

- (1) An amount that a person derives from disposing of land is income of the person if they acquired the land—
  - (a) for 1 or more purposes that included the purpose of disposing of it;
  - (b) with 1 or more intentions that included the intention of disposing of it.

4. An amount that you derive on the disposal of land will therefore be income under s CB 6 if you acquired the land for a purpose or with an intention of disposing of it. Disposal does not have to be your dominant purpose.

5. There are two exclusions from this. Even if you acquired the land for a purpose or with an intention of disposing of it, you **will not be taxed** on the proceeds of the sale if one of these exclusions applies:

**Exclusion 1 – Residential land (s CB 16)**

If the land has a house on it, or you build one, and you occupy the house mainly as a residence, you will not be taxed on the proceeds from selling the property. This also applies if you are trustee of a trust, and a beneficiary of the trust occupies the house mainly as a residence.

Please note that you cannot use this exclusion if you have a regular pattern of acquiring and disposing of houses, or building and disposing of houses.

**Exclusion 2 – Business premises (s CB 19)**

If the land is the premises of a business, and you acquired and occupied the premises or built and occupied the premises mainly to carry on a substantial business from them, you will not be taxed on the proceeds from selling the property.

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## EXPOSURE DRAFT - FOR COMMENT AND DISCUSSION ONLY

Please note that you cannot use this exclusion if you have a regular pattern of acquiring and disposing of, or building and disposing of, premises for businesses.

### How does the purpose or intention rule relate to the 2-year "bright-line" rule?

6. The new 2-year "bright-line" rule (s CB 6A) taxes any gains from residential property that is disposed of within two years of being acquired.
7. The 2-year "bright-line" rule is **in addition** to the other land sale rules that have been in New Zealand's tax law for many years. If the proceeds from selling land are taxed under one of the other land sale rules, including the purpose or intention rule, s CB 6A is not applicable.

**Deleted:** There are special rules about when you are treated as acquiring the land for the "bright-line" rule. In a typical land purchase situation, this will be when the title is registered to you. There are some exclusions from the 2-year "bright-line" rule, including an exclusion for your main home.

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### When will the proceeds of a land sale be income under s CB 6?

8. As noted above, an amount that you derive on the disposal of land will be income under s CB 6 if you acquired the land for a purpose or with an intention of disposing of it. But remember that there are exclusions for residential land and business premises that might apply (see [5]).
9. The key things to bear in mind in deciding if s CB 6 applies are:
  - What matters is your purpose or intention **when you acquired** the land.
  - A purpose or intention of disposing of the land does not need to be the only purpose or intention you had when you acquired the land. It also does not need to be your dominant or main purpose or intention. It is enough if disposal is one of your purposes or intentions.
  - Disposing of the land has to be more than a vague idea or just a possibility or option in the future. You have to have a firm purpose or intention of disposing of the land.
  - The test of whether you had a purpose or intention of disposing of the land is subjective. But what you say your purpose or intention was will be assessed against all of the circumstances.
  - Evidence of what your purpose or intention was before you acquired the land (eg, during the whole acquisition process) can be taken into account.
  - The extent of commitments you make or steps you take shortly after you acquired the land may be relevant in testing what your subjective purpose or intention was.
  - The length of time you held the land may also be taken into account, and if you have a pattern of acquiring and disposing of land within relatively short timeframes, that is likely to be relevant.
  - The onus is on you to show that you did not acquire the land for a purpose or with an intention of disposing of it.

(See for example: *CIR v Boanas* (2008) 23 NZTC 22,046 (HC), *Case N59* (1991) 13 NZTC 3,457, *Harkness v CIR* (1975) 2 NZTC 61,017 (SC), *Anzamco Ltd (in liq) v CIR* (1983) 6 NZTC 61,522 (HC), *Case Y3* (2007) 23 NZTC 13,028 and *Jurgens & Doyle v CIR* (1990) 12 NZTC 7,074 (HC)).

### When do you test what my intention was?

10. It is your purpose or intention when you **acquired** the land that is relevant.
11. Land is normally acquired for s CB 6 purposes on the date you enter into a binding sale and purchase agreement to buy the land (even if this is subject to conditions, eg, finance, or obtaining a satisfactory LIM or building report). The

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## EXPOSURE DRAFT - FOR COMMENT AND DISCUSSION ONLY

time of acquisition may be different in particular circumstances, for example, if you acquired the land through exercising an option (see s CB 15B).<sup>1</sup>

### **What if I did not have any firm intention when I bought the land?**

12. If at the time you acquired the land you did not have a firm purpose or intention, you will not ~~have a purpose or intention of disposal. You will not~~ be taxed on the proceeds of its eventual sale under s CB 6.
13. However, if the Commissioner questions whether you acquired the land with a purpose or intention of disposal, remember that the onus is on you to show that you did not. What you say your purpose or intention was will be assessed against all of the circumstances.

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### **What if my intention changes and I decide not to sell the land?**

14. The only thing that is relevant is your purpose or intention when you **acquired** the land. If you acquired the land with a purpose or intention of disposing of it, but change your mind and decide to do something else (eg, rent the property out), you will still be taxed on the proceeds if you eventually sell it.

### **What if I own the land for more than 10 years before I sell it?**

15. A common misconception is that if you hold the land for more than 10 years you will not be taxed on the sale proceeds. This is not true. If you acquired the land with a purpose or intention of disposal, s CB 6 will apply to tax the proceeds **whenever** you eventually sell the land (subject to the exclusions noted at [5]).

### **What if I have rented out the property and paid tax on the rental income?**

16. ~~If you acquired the land with a purpose or intention of disposing of it, but change your mind and decide to rent the property out instead, you will still be taxed on the proceeds when you eventually sell it. This is the case even though the rental income will have been subject to tax. The rental income and the proceeds on the sale are both taxed under the Act (see s CC 1).~~

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### **What if I only sell some of the land?**

17. It does not matter if you divide the land and sell only some of it at any one time – you will still be taxed on the proceeds of all of the land whenever it is sold. Similarly, it does not matter if you sell the land you acquired together with some other land. The proceeds on the sale of the original piece of land you acquired with a purpose or intention of disposal will be taxed under s CB 6 irrespective of what you subsequently do with the land or its boundaries (see ss CB 6(3) and CB 23B).

### **What if a trust or company buys the property?**

18. Section CB 6 can apply regardless of whether the property is acquired by an individual person or an entity such as a trust or company. If the owner is a trust or company, it is generally the purposes or intentions of the trustees or directors that are relevant in deciding if s CB 6 applies.

### **Does this only apply to sales of freehold land?**

19. No. "Land" is defined in the Act as including any estate or interest in land, and as including an option to acquire land or an estate or interest in land. You could be taxed under s CB 6 if you dispose of any land interest, not just the freehold estate. For example, you could be taxed if you dispose of a leasehold, unit title

<sup>1</sup> Note that these rules about when land is acquired apply for disposals of land on or after 22 November 2013. See [Tax Information Bulletin Vol 26, No 7, August 2014](#).



## EXPOSURE DRAFT - FOR COMMENT AND DISCUSSION ONLY

or cross-lease interest, an option to acquire land, or an equitable interest in land (eg, by transferring the right to acquire land under a sale and purchase agreement to someone else).

### Can I gift the land instead so I do not have to pay tax?

20. No. Property cannot be gifted to get around paying tax on its sale. The Act would treat a gift of land you acquired with a purpose or intention of disposal as being made at market value. You would be subject to tax on that amount, less any allowable deductions (see ss FC 1 and FC 2).

### Can I get any tax deductions?

21. Yes. If s CB 6 taxes you on the proceeds of selling land, you will get a deduction for the cost of the land and any capital improvements you make to it, as those costs are incurred in deriving the income under s CB 6 and are not private in nature (ss DB 23, DA 1 and DA 2(2)). The deduction is taken in the income year in which you dispose of the land (see s EA 2).
22. You will also be able to deduct other expenditure, such as interest on money borrowed to purchase the land, insurance, and repairs and maintenance. Deductions for these expenses will be allowed as they are incurred in deriving the income under s CB 6 and are not private in nature (ss DA 1, DA 2 and DB 6).

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### Other taxing provisions that could apply if s CB 6 doesn't

23. As well as the 2-year "bright-line" rule (see from [6]) and s CB 6 (see from [8]), there are a number of other land sale rules in the Act that might tax you on the sale proceeds. For example, you might be taxed on the proceeds of selling land if:
- you acquired the land for the purpose of a business (carried on by you or by an associated person) of dealing in land, developing land, dividing land into lots, or erecting buildings (s CB 7);
  - you dispose of the land within 10 years of acquiring it, if at the time you acquired it you were (or were associated with someone who was) in the business of dealing in land, or developing or dividing land (ss CB 9 and CB 10);
  - you dispose of the land within 10 years of completing improvements to it, if at the time you acquired it you were (or were associated with someone who was) in the business of erecting buildings (s CB 11); or
  - the land was part of an undertaking or scheme, meeting certain criteria, that involved the development of land or the division of land into lots (ss CB 12 and CB 13).
24. There are exclusions from each of these rules that might be relevant to you.

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### What if I have possibly taken an incorrect tax position for past property sales?

25. If you think you may have taken a tax position for property sales in past tax years that is different from the Commissioner's position on how these provisions apply, we suggest you discuss the matter with your tax advisor, or us, and consider making a voluntary disclosure.

### Examples

26. The following examples are included to assist in explaining the application of the law. The examples do not consider the criteria for the exclusions to s CB 6 in any great detail, as they clearly do not apply in any of the circumstances considered. Importantly, the examples do not consider whether any of the other land sale

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rules in the Act apply. If they did apply in any of the Examples, taxable income would arise.

**Example 1 – Change of purpose or intention between contract and settlement**

27. On 10 September 2015, Tabitha and Jono entered into a sale and purchase agreement to buy a house for \$2m. They planned to move into the house with their three children. On 21 September 2015, before settlement of the purchase, Tabitha and Jono were approached with an unsolicited offer to purchase the property for \$2.25m. Tabitha and Jono decided that this offer was too attractive to turn down, confident they could find another equally desirable family home for that amount. Tabitha and Jono therefore accepted the offer on 23 September 2015, entering into a sale and purchase agreement to sell the house. Tabitha and Jono's purchase of the property was settled on 25 September 2015, and their sale of the property was settled the following week.

29. The proceeds on the sale are therefore not income to Tabitha and Jono under s CB 6.

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**Example 2 – Change of purpose or intention after acquisition, and property held for over 10 years**

30. On 11 October 2005, Laura and Connor entered into a sale and purchase agreement to purchase a property that they intended to renovate and on-sell. They advised their bank of this, as they needed to borrow sufficient funds to pay for the renovations. The purchase of the property was settled on 30 October 2005, and Laura and Connor started the renovations. After the renovation work was complete, Laura and Connor decided not to sell the property at that time, but to rent it out instead. Laura and Connor have paid tax on the rental income. In 2015, Laura and Connor decided to sell the property, and they did so on 4 December 2015.

31. For the purposes of s CB 6, Laura and Connor acquired the land on 11 October 2005, when they entered into the sale and purchase agreement to buy the property. At that time, their intention was to renovate the house and sell it. It does not matter that Laura and Connor subsequently changed their minds and decided to rent the property out instead of selling it. At the date they acquired the property, their purpose or intention was to dispose of it.

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32. Neither the residential exclusion (s CB 16) nor the business exclusion (s CB 19) apply, because Laura and Connor did not live in the property or carry on a business from it.

33. The proceeds on the sale of the property are therefore income to Laura and Connor under s CB 6.

34. It is not relevant that the rental income was subject to tax – the Act taxes rental income as well as the proceeds on the sale of the property.

35. It is not relevant that Laura and Connor held the property for more than 10 years before selling it. If land is acquired with a purpose or intention of disposal, the proceeds will be taxed whenever the property is eventually sold.

36. Laura and Connor can get a deduction against the sale proceeds for the amount they paid to acquire the property and for the cost of any renovations that were capital in nature. In each year they owned the property, they will also have been allowed to deduct the interest on the money they borrowed to purchase the property and undertake the renovations, the cost of insurance on the property, and the cost of any repairs and maintenance on the property.

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**EXPOSURE DRAFT - FOR COMMENT AND DISCUSSION ONLY**

**Example 3 – Purpose or intention to be assessed against all of the circumstances**

37. Taj acquired 28 properties over a 10-year period – all before 1 October 2015. Twenty-three of those properties have been sold to date. Taj considers that none of those sales give rise to income under s CB 6, stating that all of the properties were acquired for long-term rental. Taj states that the twenty-three properties in question were only sold due to financial pressure, the cost of servicing the mortgages, difficult tenants, or because of unsolicited offers to purchase the properties. Taj states that any renovation work done on the properties was for the purpose of deriving higher rental income.
38. However, all of the twenty-three properties were on-sold within relatively short periods after their acquisition, most of them after some renovation work. The average time the properties were held is approximately one year. Ten of the properties were held for less than six months. After each of the twenty-three properties was sold, a new property was purchased within an average of six months. Taj has only returned rental income from two of the properties.
39. ~~The test of whether a taxpayer had a purpose or intention of disposing of land when they acquired it is subjective. However, a person's stated purpose or intention needs to be assessed against all of the circumstances.~~
40. In this case, Taj's explanations for the sales are not supported by the circumstances as a whole. None of the properties were held for long-term rental purposes, which is what Taj says they were acquired for. Indeed, rental income was only returned from two of the properties. The explanations for the sales are not supported by the evidence. The fact that new properties were purchased within an average of six months after each sale undermines Taj's assertion that the sales were due to financial pressure and the cost of servicing the mortgages. The pattern of purchases, renovation (in most cases) and relatively fast re-sale of the properties without them having been rented out (for the most part) indicates that Taj acquired the properties with a purpose or intention of disposing of them.
41. Neither the residential exclusion (s CB 16) nor the business exclusion (s CB 19) apply in respect of any of the properties, because Taj did not live in any of them or carry on a business from any of them.
42. Therefore, the Commissioner considers that the proceeds on the sales of the twenty-three properties in question are income to Taj under s CB 6.
43. Taj can get a deduction against the sale proceeds for the amounts he paid to acquire the properties and for the cost of any renovations that were capital in nature. Taj will also be allowed to deduct the interest on the money he borrowed to purchase the properties and undertake the renovations, the cost of insurance on the properties, and the cost of any repairs and maintenance on the properties.

**Deleted:** <#>The 2-year "bright-line" rule does not apply to the sales of the properties in question, because they were all acquired before 1 October 2015. If Taj had acquired any of the properties on or after 1 October 2015, the proceeds of the sales of those properties would be taxed under the 2-year "bright-line" if the sale was within two years of the property being acquired. It would not be necessary to consider s CB 6 for any sales taxed under the 2-year "bright-line" rule.¶

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**Example 4 – Onus on the taxpayer to show that land not acquired with a purpose or intention of disposal**

44. Hugh and Meg purchased five residential properties in 2014. They renovated the properties, and sold them in 2015 for a total profit of \$2.2m. Hugh and Meg have stated that they have relatives overseas who had applied for New Zealand residency and who intended to live in the properties. Hugh and Meg assert that the properties were only sold in 2015 because the residency applications were unsuccessful. Hugh and Meg have not provided any evidence that any relatives overseas had applied for New Zealand residency and had those applications rejected.

## EXPOSURE DRAFT - FOR COMMENT AND DISCUSSION ONLY

45. If the Commissioner questions whether you acquired the land with a purpose or intention of disposal, the onus is on you to show that you did not.
46. Hugh and Meg purchased five properties that they renovated and sold for a profit in a short space of time. They have not provided any evidence that any relatives overseas had applied for New Zealand residency and had those applications rejected. In these circumstances, the Commissioner is not satisfied that Hugh and Meg did not acquire the properties with a purpose or intention of disposal. There is no evidence to support their stated purpose of acquiring the properties as future homes for relatives seeking residency.
47. Neither the residential exclusion (s CB 16) nor the business exclusion (s CB 19) apply in respect of any of the properties, because Hugh and Meg did not live in any of them or carry on a business from any of them.
48. The Commissioner therefore considers that the proceeds on the sales of the properties are income to Hugh and Meg under s CB 6.
49. Hugh and Meg can get a deduction against the sale proceeds for the amounts they paid to acquire the properties and for the cost of any renovations that were capital in nature. They will also be allowed to deduct the interest on the money they borrowed to purchase the properties and undertake the renovations, the cost of insurance on the properties, and the cost of any repairs and maintenance on the properties.

**Deleted:** <#>The 2-year "bright-line" rule does not apply to the sales of the properties in question, because they were all acquired before 1 October 2015. If Hugh and Meg had acquired any of the properties on or after 1 October 2015, the proceeds of the sales of those properties would be taxed under the 2-year "bright-line" if the sale was within two years of the property being acquired. It would not be necessary to consider s CB 6 for any sales taxed under the 2-year "bright-line" rule.¶

**Deleted:** that were not capital in nature

### Example 5 – More than one purpose or intention

50. Chris purchased a property in August 2012. The property was marketed as being an attractive investment – ideal as a rental property, and expected to have "great annual capital growth". Chris decided to buy the property to rent it out for three to five years, by which stage he hoped to be able to realise a capital gain on the property. Chris has paid tax on the rental income. He sold the property in October 2015 for a sizeable profit.
51. An amount that a person derives on the disposal of land will be income under s CB 6 if they acquired the land for a purpose or with an intention of disposing of it. A purpose or intention of disposing of the land does not need to be the **only** purpose or intention the person had when they acquired the land. It also does not need to be their dominant or main purpose or intention. It is enough if disposal is one of their purposes or intentions.
52. Chris invested in the property in question because he expected it to have great annual capital growth, and it could be rented out in the meantime. He purchased the property with the purpose of renting it out in the short-medium term (three to five years) and then selling it to realise the expected capital gain.
53. It does not matter that Chris acquired the property for more than one purpose, and disposal was only one of those purposes. When he acquired the property, Chris had a firm purpose of disposing of it in three to five years to hopefully make a capital gain.
54. Neither the residential exclusion (s CB 16) nor the business exclusion (s CB 19) apply in respect of the property, because Chris did not live in it or carry on a business from it.
55. The proceeds on the sale of the property are therefore income to Chris under s CB 6.
56. It is not relevant that the rental income was subject to tax – the Act taxes rental income as well as the proceeds on the sale of the property.

**Deleted:** <#>The 2-year "bright-line" rule does not apply to the sale of the property, because it was acquired before 1 October 2015. Even if the property had been acquired on or after 1 October 2015, the 2-year "bright-line" rule would not apply because the property was not sold within two years of being acquired. Therefore, in those circumstances it would still be necessary to consider s CB 6.¶

**Deleted:** was attracted to invest

**Deleted:** it was

## EXPOSURE DRAFT - FOR COMMENT AND DISCUSSION ONLY

57. Chris can get a deduction against the sale proceeds for the amount he paid to acquire the property and for any capital improvements he made to the property. In each year he owned the property he will also have been allowed to deduct the interest on the money he borrowed to purchase the property, the cost of insurance on the property, and the cost of any repairs and maintenance on the property.

Deleted: that were not capital in nature

*Draft items produced by the Office of the Chief Tax Counsel represent the preliminary, though considered, views of the Commissioner of Inland Revenue.*

*In draft form these items may not be relied on by taxation officers, taxpayers, and practitioners. Only finalised items represent authoritative statements by Inland Revenue of its stance on the particular issues covered.*

## References

### Subject references

Income tax, sale of land, purpose or intention of disposal

### Legislative references

Income Tax Act 2007 – ss CB 6A, CB 6, CB 7, CB 9, CB 10, CB 11, CB 12, CB 13, CB 15B, CB 16, CB 19, CB 23B, CC 1, DA 1, DB 6, DB 7, DB 23, EA 2, FC 1 and FC 2

### Case references

*Anzamco Ltd (in liq) v CIR* (1983) 6 NZTC 61,522 (HC)  
*Case N59* (1991) 13 NZTC 3,457  
*Case Y3* (2007) 23 NZTC 13,028  
*CIR v Boanas* (2008) 23 NZTC 22,046 (HC)  
*Harkness v CIR* (1975) 2 NZTC 61,017 (SC)  
*Jurgens & Doyle v CIR* (1990) 12 NZTC 7,074 (HC)