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31 January 2013

Team Manager, Technical Services
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Via email **public.consultation@ird.govt.nz**

Dear Manager]

INCOME TAX – RESIDENCE
Submission re IRD Draft Interpretation Statement
Your Reference: INS0117

We hereby provide a submission in respect of the above draft interpretation statement released by IRD in December 2012 for comment by 31 January 2013.

General Comment -Over reliance on Case Q55 and re-analysis required

In our view, IRD is inappropriately seeking to amend the implications of settled case law in the area of Permanent Place of Abode ("PPOA").

In particular, the draft Interpretation Statement refers to case *Case Q55* (1993) 15 NZTC 5,313 "Case Q55" some eleven separate times.[1]

Case Q55 was decided in New Zealand's lowest form of judiciary and, even more importantly, involved an extreme fact scenario.

Accordingly, the judicial comments made therein may well be appropriate *ratio decidendi* specific to those extreme facts, but are not particular relevant, and of little or no precedential value, when considering the majority of factual scenarios where an individual's residency is required to be determined.

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[1] See Draft Interpretation Statement INS0117 paragraphs 18, 19, 20, 21, 25, 26, 27, 29 x 2, 33 and 38.

We are particularly concerned that (as we have experienced previously) IRD staff will take an aggressive approach, asserting that retention of a rental property, particularly when previously or subsequently occupied by the taxpayer or an associated party, is an overwhelming indicator of have retained a 'permanent place of abode' – and not the more appropriate conclusion that it may indicate the potential availability of a dwelling.

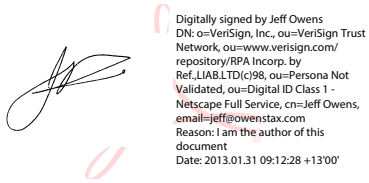
Reconsideration of the alleged established principles from Case Q55 should be undertaken, with particular emphasis placed on decisions of higher judiciaries and those involving more typical fact scenarios.

Following that reconsideration, all examples will need to be revisited and updated

We attach our detailed analysis at Appendix 1.

We trust that our submission is helpful.

Yours faithfully



Jeff Owens
Director

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APPENDIX 1 Specific Comments

1.1 PPOA - Requirement for "Available Dwelling"

1.1.1 Observation

The draft Interpretation Statement takes the specific position, contrary to PIB 160, that in order to have retained a 'permanent place of abode', a person must have a particular place of abode that is an "available dwelling".[2] The draft Interpretation Statement purportedly relies on two cases to support this proposition - Case F138 (1984) 6 NZTC 60,237 and Case Q55 (1993) 15 NZTC 5,313.

1.1.2 Required Amendment / Further Analysis re F138

Case F138 does not support the contention that a taxpayer is required to have an available dwelling and there is no such comment or evidence of any analysis made by the judiciary in that regard. Rather the court noted that *"I think O's permanent place of abode during the period was in New Zealand. This is so whether or not one has regard to the quality of his person or of his property." [Emphasis added]*

The ratio decidendi of the court did not outline a requirement to first have an available dwelling before considering other aspects of the PPOA test. Rather, the court referred to and accepted wide definitions of *resident* and *abode* that did not stipulate any necessity of a physical dwelling being available. The court also concluded that the taxpayers intention (to temporarily be absent from NZ and to then return) and the objective facts *"singularly and together […] persuade me […] that O's permanent place of abode during the period was in New Zealand". [Emphasis added].* That is, the mere intention to be away from New Zealand temporarily and to then return is *singularly* sufficient to establish that a PPOA was retained in NZ. I.e. there is no requirement for an available dwelling in order for a PPOA to be established.

The availability of a dwelling was only one of 12 factors relevant factors listed in the judgement.

1.1.3 Required Amendment / Further Analysis re Q55

Case Q55 similarly should not be used as support for the contention that a taxpayer is required to have an available dwelling. Judicial comments made to that effect were obiter and the fact scenario in that case was extreme.

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[2] See Draft Interpretation Statement INS0117 first bullet point of differences to PIB 180 of June 1989, and paragraph 19.

In that case the judiciary specifically considered initially that the *"The issue is whether the New Zealand city property or home or, perhaps, the New Zealand city, could be regarded as his permanent place of abode while he and his wife were overseas".* Clearly, it was contemplated at that initial point in the case that the existence of a PPOA may not require a specific particular dwelling to be available.

Based on the extreme fact scenario of that case (where the taxpayer had lived in that house for the previous 51 years, intended to return to it, and did so), the court subsequently found that a dwelling was available and a PPOA did exist.

Justice Barber has then gone on to comment that:

> *"I do not think that a durable connection with a locality alone could create "a permanent place of abode" where a dwelling is not owned or tenanted or otherwise available such as the house of a parent, or relative, or friend. I consider that the phrase "has a permanent place of abode" requires, inter alia, the availability of a place in which to dwell…".*
>
> *"I think that the strength of a person's ties with New Zealand is the paramount factor in assessing residency but those ties must include the availability on a permanent basis (continuing indefinitely) of a place in which to dwell and sleep if that person is to have a permanent place of abode somewhere in New Zealand. The enduring availability of a dwelling is a fundamental criterion to having a permanent place of abode,…".*

It is regrettable that, having found that the taxpayer had many substantial ties to New Zealand, including the availability of a dwelling, Justice Barber then (at least in the written judgment) failed to provide any support for his conclusion that the enduring availability of a [specific] dwelling is a *fundamental criterion* to having a permanent place of abode. This is particularly so given:

a) the wide definitions of *abode* (that do not limit the definition to a particular dwelling) that were cited earlier in the case with approval by Justice Barber, and

b) that having found that the taxpayers dwelling was in fact available to him, any subsequent consideration as to whether the availability of a dwelling was a "fundamental criterion" in establishment of a PPOA were merely *obiter dicta* and not *ratio decidendi.*

It is further and similarly regrettable that having apparently failed to outline the reasoning for his obiter dicta conclusions on this aspect, Justice Barber did not then distinguish his reasoning from the established principles and judicial comments of the Full Federal Court of Australia in FC of T v Applegate 79 ATC 4307 and the Supreme Court of New Zealand (now the High Court) in Geothermal Energy New Zealand Ltd v C of IR (1979) 4 NZTC 61,478.

1.1.4 Required Amendment / Further Analysis re Applegate

The meaning of the concept of permanent place of abode was considered by the Full Federal Court of Australia in FC of T v Applegate 79 ATC 4307. This decision (unanimously held by three Federal Court judges) it is clear that the concept of place of abode does not refer merely to a specific dwelling or home but acknowledges that is one of a number of tests. See the judgement of Northrop J:

> *"The phrase ``place of abode'' may have many meanings, it can refer to the building or place where a person sleeps and it can refer to the building or place where he is usually found, for instance, ``his place of business'', see Price v. West London Investment Building Society (1964) 2 All E.R. 318 per Danckwerts L.J. at p. 321. The phrase is often used as being synonymous with the word ``residence'' see, for example, Levene v. I.R. Commrs. (1928) A.C. 217 and I.R. Commrs. v. Lysaght (1928) A.C. 234 . In the present case there can be no doubt that whatever meaning is given to the phrase, during the period in question the taxpayer's ``place of abode'' was outside Australia. During that period he did not reside in Australia. He had no residence in Australia. He had no home in Australia. He did not carry on business or work in Australia. He received no income from sources within Australia. …"*

The court went on to determine the extension of the phrase by the addition of the word "permanent".

> *It follows, therefore, that the real issue is whether, during the period in question, the taxpayer's place of abode outside Australia was permanent or not.*
>
> *The word ``permanent'' can have many shades of meanings. This is illustrated by a reference to the Shorter English Oxford Dictionary. And as was said by du Parcq L.J. in Henriksen (Inspector of Taxes) v. Grafton Hotel Ltd. (1942) 2 K.B. 184 at p. 196:*
>
> *```Permanent' is indeed a relative term, and is not synonymous with `everlasting'."*
>
> *The word ``permanent'' must be construed according to the context in which it appears, see per Lord Evershed in McClelland v. Northern Ireland General Health Services Board (1957) 2 All E.R. 129 at p. 140.*

> *In the present case the phrase ``permanent place of abode'' appears in a taxing statute by which income tax is levied on income derived during a financial year. …. The tax is assessable on gross income received on an annual basis and is assessed on an annual basis. The word ``permanent'' as used in para. (a)(i) of the extended definition of ``resident'', must be construed as having a shade of meaning applicable to the particular year of income under consideration. In this context it is unreal to consider whether a taxpayer has formed the intention to live or reside or to have a place of abode outside of Australia indefinitely, without any definite intention of ever returning to Australia in the foreseeable future."*

It is clear from this case that there is no fundamental criterion for the existence or availability of an identifiable dwelling.

1.1.5 Required Amendment / Further Analysis re Geothermal Energy

In the Geothermal Energy case (Geothermal Energy New Zealand Limited v Commissioner of Inland Revenue (1979) 4 NZTC 61,478 Supreme Court of New Zealand. 14 September 1979) the concept of residency was considered. In the case it was suggested by counsel for the taxpayer that legislation referring to "his home is in New Zealand" had previously been incorrectly interpreted to refer to a test of whether there had been "retention of a home" in New Zealand.

That this wording was incorrectly interpreted appears to have been accepted by the Court.

> *"If, as appears to be the situation in this case, some overseas employees own houses in New Zealand, possibly in which they lived before going overseas and possibly in which they intend to resume living on their eventual return to New Zealand, which are let to tenants, that does not mean in my opinion they are thereby ipso facto resident in New Zealand but rather that they may be in the same position as any other overseas resident who has an investment in property here. Some support to this opinion is given in May v May (1881) 44 L.T. 412 where a testator directed in his will that his widow might reside rent-free in his then residence during her life. For some years she actually lived in the house herself but then she moved out and let it. The question was whether that provision in the will entitled her to let the home or to retain the rents. Fry J. held that letting the house to tenants was the antithesis of being resident there. In very broad terms I consider that once a person lets his former dwelling place and moves away from it with his family it is not his "home" any more — at least until he and his family move back into it.*

> *Finally, because ownership of property is not to be confused with the concept of fiscal "residence" (see I.R. Commrs. v. Lysaght (supra) per Viscount Sumner at p. 244) and provided that after letting the house he removes overseas with his family, again in broad terms in my view a man will not continue to be resident in New Zealand merely because he owns a property here." [Emphasis added]*
>
> *…*
>
> *"Home" under sec. 241 should not be regarded as synonymous with the ownership of any interest in a house or property. It should in my opinion be construed qualitatively. [Emphasis Added].*

In this case the court also commented that if, in respect of the meaning of "home" it was intended to refer to the different concept of "permanent home" (and acknowledging that "in that sense making it similar to the concept of domicile") as follows:

> *"For completeness I would like to add that had the Legislature meant the "permanent home" of the taxpayer in sec. 241(1) then in my respectful view it only had to say so."*

Subsequent legislative amendments to refer to "permanent place of abode" have presumably been included with both the decision in Applegate and the courts comments above in mind.

1.1.6 Required Amendment / Further Analysis re Brightline Test

The draft interpretation statement refers a number of times to there being "no bright line test".[3]

However, asserting that there is a fundamental criterion for a specific dwelling to be in existence would in fact be directly imposing a negative bright line test. I.e. failure to have a specific dwelling available to the taxpayer would prevent that taxpayer being considered to have a PPOA in New Zealand.

The relevant case law clearly supports, as noted in the draft Interpretation Statement that there is to be no bright line test for either existence or absence of a PPOA. On that basis the notion of dwelling availability being a fundamental criterion rather than an indicative factor is simply incorrect.

[3] See Draft Interpretation Statement INS0117 introductory bullet point of differences to PIB No 180 of June 1989 re Examples, paragraph 10 and Attachment – Comparison to PIB No 180.

1.1.7 Required Amendment / Further Analysis re Avoidance Opportunities

If the availability of a dwelling was treated as a fundamental criterion to having a permanent place of abode, taxpayers could readily subvert the individual residency tests.

For example a taxpayer with substantial ties, global investments, and employment in New Zealand could readily be considered a non-resident under this interpretation by simply:

a) Remaining absent from New Zealand for 325 days (and therefore being considered prima facie non-resident under the personal presence/.absence tests),

b) Ensuring they did not have any dwelling available to them in New Zealand (by selling property and/or breaking any leases and therefore not being considered to have a PPOA in New Zealand).

This would provide a significant risk to revenue for taxpayers seeking to temporarily avail themselves of the advantages of non-residency. They could "leave in January and still be home in time for Christmas".

Such an outcome was clearly not intended by the legislature.

The *obiter dicta* portion of the judiciary comment in Q55 has not been viewed as precedential in nature by taxpayers or the IRD for nearly twenty years. There appears no merit in seeking to now treat it as such.

1.2 Relevance of PPOA outside New Zealand

1.2.1 Observation

The draft Interpretation Statement takes the specific position that "it does not matter if a person also has a permanent place of abode outside New Zealand".[4]

1.2.2 Required Amendment / Further Analysis re foreign PPOA relevance

Whilst strictly speaking the existence of any foreign PPOA is not determinative for the existence of a PPOA within New Zealand, the concept of permanence requires consideration of the taxpayer's state of mind and the objective facts surrounding the place of abode.

In Applegate, Fisher J stated that

[4] See draft Interpretation Statement INS0117 paragraph 17.

> *"It [the phrase PPOA] connotes a more enduring relationship with the particular place of abode than that of a person who is ordinarily resident there or who has there his usual place of abode. Material factors for consideration will be the continuity or otherwise of the taxpayer's presence, the duration of his presence and the durability of his association with the particular place."*

Accordingly, relying as it does on a taxpayer's intentions and other factors, the existence of a foreign PPOA ***does*** matter and will certainly require consideration when determining whether a PPOA exists in New Zealand.

The use of the term "permanent" within the phrase imports, in almost all conceivable cases, a practical mutual exclusivity on having more than one PPOA.

We note that consideration of any such foreign PPOA was specifically required in case Q55 as one of the criteria for establishing a PPOA in New Zealand *"Whether the objector established a permanent place of abode out of New Zealand".*

Clearly the reference within the draft Interpretation Statement requires amendment.

1.3 Relevance of Fixed vs Periodic Leasing Arrangement

1.3.1 Observation

The draft Interpretation Statement refers to the immediacy and ease with which a person could occupy or reoccupy a dwelling.[5]

1.3.2 Required Amendment / Further Analysis re nature of lease

The draft Interpretation Statement refers to the "enduring availability" of a dwelling but mistakenly and quite inappropriately refers to the immediacy or ease with which the property could be occupied or reoccupied.

In Case Q55 the taxpayer had entered into a fixed term lease and yet this was found to be a dwelling available for the occupation of the taxpayer. Barber J referred to the potential availability for the taxpayers occupation; implying that normal commercial fixed term or periodic leases for residential property would not be likely to alter the perceived availability or otherwise of a dwelling.

Further elaboration is required here to ensure the Interpretation Statement clarifies that the relevant factor is the surrounding circumstances of a particular dwelling, rather than the particular form of any lease to a third party.

[5] See draft Interpretation Statement INS0117 paragraph 23.

In Example 15 the draft Interpretation Statement includes reference to a lease terminable on short notice. This requires expansion or modification to specifically address the different implications, if any, that a fixed term lease for the 15 month period of Stacey's absence would involve.[6]

We note that the draft Interpretation Statement includes an almost identical mirror example at Example 17. The only apparent material difference being that in Example 15 the taxpayers dwelling is rented on a periodic lease, whereas in Example 17 it is a fixed term lease.[7]

Currently, we note that both examples appear to inappropriately conclude in favour of IRD in New Zealand.

Neither example appears to refer to the potential availability for personal occupation as required by case Q55.

Clearly further analysis, and we suggest a closer integration, of the two examples is required.

1.4 Relevance of Previous Occupation

1.4.1 Observation

The draft Interpretation Statement states that *"Whether (or the extent to which) the person has lived in the dwelling will be a relevant factor to take into account in assessing the availability of the dwelling, but it is not essential that they have lived in the particular dwelling before"*.[8]

1.4.2 Required Amendment / Further Analysis re Previous Occupation

This statement is without balance and requires inclusion of an alternative hypothesis. That is, the paragraph should also clearly state that a rental investment that is held and has always been treated as a rental investment should

a) not be considered available for occupation by the taxpayer and

b) even if it were so considered available should be only one of many other factors considered when determining whether or not a PPOA exists.

[6] See draft Interpretation Statement INS0117 paragraph 164.
[7] See draft Interpretation Statement INS0117 paragraph 170.
[8] See draft Interpretation Statement INS0117 paragraph 147.

1.5 Relevance of DTA Tie Breaker Dual Home Provisions

1.5.1 Observation

The draft Interpretation Statement states that *"If it is apparent that a person who is dual resident has a permanent home available in New Zealand that will be an end to the matter unless the person can establish that they also have a permanent home available in the other country."*.[9]

1.5.2 Required Amendment / Further Analysis re DTA Tie Breaker Dual Home Provisions

This statement also provides no balance and needs to be amended to refer to both New Zealand and other countries/jurisdictions. We recommend simple wording changes as follows:

> *If it is apparent that a person who is dual resident has a permanent home available in one country or jurisdiction that will be an end to the matter unless the person can establish that they also have a permanent home available in the other country/jurisdiction.*

[9] See draft Interpretation Statement INS0117 paragraph 24.