

**EXPOSURE DRAFT - FOR COMMENT AND DISCUSSION ONLY | HUKIHUKI HURANGA
- MŌ TE TĀKUPU ME TE MATAPAKI ANAKE**

Deadline for comment | Aukatinga mō te tākupu: **14 February 2025**

Please quote reference | Whakahuatia te tohutoro: **PUB00519**

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QUESTIONS WE'VE BEEN ASKED | PĀTAI KUA UIA MAI

Can section CB 3 apply to amounts derived from the disposal of land?

Issued | Tukuna: Issue date style

QB XX/XX

This question we've been asked considers whether s CB 3 of the Income Tax Act 2007 can apply to amounts derived from the disposal of land. Section CB 3 provides that an amount derived from an undertaking or scheme for the purpose of making a profit is income of a person.

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

Key provisions | Whakaratonga tāpua

Income Tax Act 2007 – s CB 3

Question | Pātai

Can section CB 3 apply to amounts derived from the disposal of land?

Answer | Whakautu

Section CB 3 can apply to amounts derived from the disposal of land as part of a profit-making undertaking or scheme. The land sale rules are not a code and other provisions of the Act, including s CB 3, can potentially apply to tax amounts derived from the disposal of land.

Section CB 3 does not, however, apply to any amount derived from an undertaking or scheme involving the development of land or division of land into lots. This is because of the interpretive presumption that specific provisions override general provisions. Section CB 3 is a general provision relating to undertakings or schemes, whereas ss CB 12 and CB 13 are specific provisions relating to undertakings or schemes of a particular type – those involving land development or division.

Other than for an undertaking or scheme involving the development of land or the division of land into lots, it is open to the Commissioner to argue that s CB 3 applies as an alternative to the land sale rules. In most instances where no land sale rule applies, however, it will also be the case that s CB 3 cannot apply because the land is likely to be a capital asset and the amount derived the mere realisation of that capital asset.

Key terms | Kīanga tau tāpua

Land sale rules means the provisions relating to disposals of land in ss CB 6A to CB 23B.

Explanation | Whakamāramatanga

Background

1. Section CB 3 provides that an amount derived from an undertaking or scheme for the purpose of making a profit is income of a person.
2. It has been suggested that the land sale rules are a code, meaning that amounts derived from the disposal of land are subject to tax only if one of those rules applies and that other provisions such as s CB 3 cannot apply to disposals of land. We have been asked what the Commissioner's view on this is.

Can section CB 3 apply to amounts derived from the disposal of land?

3. Based on the scheme of the Act, legislative history and relevant case law, the Commissioner considers that s CB 3 can potentially apply to amounts derived from the disposal of land as part of a profit-making undertaking or scheme. The land sale rules are not the only provisions of the Act that could apply to tax amounts derived from the disposal of land. In other words, the land sale rules are not a code. In particular, there is no clear indication that Parliament intended that the land sale rules would apply to tax the disposal of land to the exclusion of all other provisions of the Act.
4. The plain words of s CB 3, together with the scheme of the Act, suggest that the section can apply to the disposal of land. This is for the following reasons:
 - There is no indication on the clear words of s CB 3 that it was not intended to apply to land. Rather, the section states that it applies to any amount derived from a profit-making undertaking or scheme.
 - Similarly, no provision in the land sale rules states that the land sale rules are the only provisions that can apply to an amount derived from the disposal of land.
 - Schematically, the headings in Part C do not suggest any restriction to the scope of s CB 3, or that the land provisions were intended to be a code. Rather, the headings are included to provide assistance with navigation of the Act. Part C is titled "Income". Subpart CA is headed "General rules" and subpart CB "Income from business or trade-like activities". Section CB 3 is under its own subheading of "Schemes for profit". If the subheading "Land" before ss CB 6A to CB 23B was intended to make those provisions a code in relation to amounts derived from the disposal of land, there would be no ability for such amounts to fall within the general provisions (for example, s CA 1(2) (income according to ordinary concepts)).
 - Further, if the "Land" subheading was intended to make those provisions a code for taxing disposals of land, presumably the same logic would apply to other subheadings in subpart CB. This would suggest, for example, that the subheading "Personal property" before ss CB 4 and CB 5 was intended to make those provisions a code for taxing amount derived from the disposal or personal property. Such an interpretation would severely limit the scope of s CB 3, as it would not apply to any undertaking or scheme involving the disposal of any kind of property. There is no question that s CB 3 can apply to the disposal of personal property.

5. In addition, there is case law support for s CB 3 applying to land.¹
6. Finally, it is not clear from the legislative history that Parliament intended the land sale rules to be a code, or that Parliament intended to remove land from the scope of what is now s CB 3. While it is clear that the 1973 amendments resulting in the introduction of many of the land sale rules were intended to overcome limitations placed on the earlier provision by the courts, it is not clear that the amendments were intended to result in s CB 3 not having any potential application to land disposals.

When does section CB 3 apply to amounts derived from the disposal of land?

7. Although s CB 3 appears to have broad application, not all undertakings or schemes involving the disposal of land are within the scope of the provision. This is because the courts have put interpretive glosses on s CB 3.
8. In summary, of particular relevance to land disposals, the courts have held that s CB 3 only applies where:
 - there is business-like activity (but not a business);²
 - the activity is carried on for the dominant purpose of making a profit;³ and
 - the amount is not derived from the mere realisation of a capital asset.⁴
9. One concern raised about s CB 3 applying to land disposals is that the exclusions in the land rules are not relevant when applying s CB 3. Those exclusions are for residential land (s CB 17), business premises (s CB 20), farm land (s CB 21), and investment land (s CB 23). It is likely that land that falls within any of those exclusions would almost always be capital in nature, as a person's home, business premises or investment property is almost always a capital asset. This means that if one of the exclusions from the land sale rules applies, s CB 3 is unlikely to apply because of the judicial gloss that the provision does not apply to the realisation of capital assets.

¹ *TRA 009/20* [2021] NZTRA 4, *Lowe v CIR* (1981) 5 NZTC 61,006 (CA), *Dobson v CIR* (1987) 9 NZTC 6,025 (HC), *Case S86* (1996) 17 NZTC 7,538 (TRA).

² *McClelland v FCT* 70 ATC 4115 (PC); *Duff v CIR* (1982) 5 NZTC 61,131 (CA). The existence of a "business" is determined by applying the criteria in *Grieve v CIR* (1984) 6 NZTC 61,682 (CA).

³ *CIR v National Distributors Ltd* (1989) 11 NZTC 6,346 (CA). This contrasts with s CB 6, where profit need only be a purpose (or intention) for acquiring the land.

⁴ *Beetham v CIR* 72 ATC 6042 (NZSC); *Eunson v CIR* [1963] NZLR 278 (SC) at 281. See also *FCT v Whitfords Beach Pty Ltd* [1982] HCA 8.

Do any of the land sale rules exclude the operation of section CB 3?

10. Two provisions in the land sale rules deal with an amount derived from an undertaking or scheme – ss CB 12 and CB 13.
11. In summary, ss CB 12 and CB 13 apply where there is an undertaking or scheme that:
 - is not necessarily in the nature of a business;
 - involves the development of the land or division of the land into lots; and
 - for s CB 12:
 - the work is not minor; and
 - the undertaking or scheme was commenced within 10 years of acquisition of the land; or
 - for s CB 13:
 - the undertaking or scheme was commenced more than 10 years after acquisition (as s CB 13 can apply only if s CB 12 does not apply);
 - none of certain other specified land sale rules apply (all but s CB 15); and
 - the undertaking or scheme involves significant expenditure on the types of work specified in the section.
12. It is clear the scope of both sections differs from that of s CB 3 as they do not require that there be a business-like activity nor do they require a profit-making purpose.
13. On a literal reading, a significant overlap appears to exist in scope between the provisions. Where there are two provisions in an Act that deal with the same subject matter, the interpretive presumption that specific provisions override general provisions (*specialia generalibus derogant*) may be relevant.
14. Sections CB 12 and CB 13 are clearly more specific than the general provision in s CB 3. Sections CB 12 and CB 13 detail the circumstances where a particular type of undertaking or scheme – one involving the development of land or the division of land into lots – may be subject to tax.⁵ They cover both situations where the undertaking or scheme was commenced within 10 years of acquisition (s CB 12), and where more than 10 years have passed (s CB 13).

⁵ Unless an exclusion applies.

15. It is considered that Parliament intended ss CB 12 and CB 13 to comprehensively provide for the taxation of any disposal of land as part of an undertaking or scheme involving the development of land or the division of land into lots.
16. Because of the interpretive presumption that specific provisions override general provisions, s CB 3 does not apply to any amount derived from the disposal of land as part of an undertaking or scheme involving land development or division. This is the case even where the amount is not subject to tax under either of the more specific provisions (s CB 12 or s CB 13), whether due to an exclusion applying or the criteria in those provisions not being met.
17. For example, this means s CB 3 cannot apply to an undertaking or scheme for the development of land or the division of land into lots where:
 - the undertaking or scheme was commenced within 10 years of acquisition, but the development or division work was only minor;
 - the undertaking or scheme was commenced more than 10 years after acquisition of the land but the development or division work did not meet the significant expenditure threshold in s CB 13; or
 - either s CB 12 or s CB 13 *prima facie* applies, but one of the exclusions from the relevant taxing provision (that is, s CB 17, s CB 20, s CB 21 or s CB 23) applies to exclude the application of the taxing provision.
18. Other than in relation to ss CB 12 and CB 13, there is no reason to conclude that any of the land sale rules exclude the potential application of s CB 3. The other land sale rules do not cover the same subject matter as s CB 3, so the interpretive presumption that specific provisions override general provisions is not relevant.
19. This means that, other than for an undertaking or scheme involving the development of land or the division of land into lots, it is open to the Commissioner to argue s CB 3 as an alternative to the land sale rules.
20. While theoretically s CB 3 may apply in the alternative to a land sale rule, in most instances where no land sale rule applies it will also be the case that s CB 3 cannot apply because the land is likely to be a capital asset and the amount derived the mere realisation of that capital asset. However, there may be circumstances where that is not the case.

Examples | Taurira

Example | Taurira 1 – Specific land sale rule does not apply due to an exclusion; section CB 3 also does not apply

Sylvia is a qualified master builder and has carried on a business of erecting buildings for clients for over 20 years. Six years ago, Sylvia acquired a block of bare land and built a house on the land. Sylvia lived in the house from the time construction was complete. Sylvia has not previously lived in any of the houses she has built.

Sylvia recently moved to Australia and sold the property.

The sale of the property meets the requirements of s CB 11, as when the improvements were begun Sylvia was in the business of erecting buildings and the sale is within 10 years of the improvements being completed. However, the residential exclusion in s CB 16 applies, as the house was used by Sylvia as her residence.

Section CB 3 does not apply to the sale, as there is no undertaking or scheme carried on in a business-like manner with an intention to make a profit. The sale is the mere realisation of a capital asset.

Example | Taurira 2 – Section CB 12 applies; section CB 3 does not apply

Elisapeta purchased 10 acres of land seven years ago. She began to build her dream home on the land, but building costs exceeded her expectations and she decided to subdivide the land to help finance the construction. The land was subdivided into one lot of 3 acres with her home on it and one lot of 7 acres to sell.

Elisapeta used the professional services of a surveyor, solicitor and geotechnical engineer. She also organised a landscaper to fence between the two lots and had an earthworks company excavate a driveway to one of the lots. An arborist felled several trees and cleared the site, as this was necessary for the subdivision of the land.

Elisapeta sold the 7 acre block of land, which allowed her to complete construction of her home. The proceeds from that sale are taxable under s CB 12 because the subdivision involved development or division work that was more than minor.

As there is an undertaking or scheme involving development or division work, s CB 3 does not apply to the amount derived by Elisapeta, even as an alternative to the application of s CB 12.

Example | Taura 3 – Sections CB 12 and CB 13 do not apply and neither does section CB 3

Nic has owned a large property for over 20 years and has decided to downsize. To maximise returns from the sale of the property, Nic decides to subdivide the land and sell it as four separate lots.

As a condition of the subdivision consent, the council required Nic to construct a paved entranceway to the subdivided lots, with additional drainage to minimise the risk of flooding. The development work required by the council was straightforward and the cost to complete it was minimal.

Section CB 12 does not apply as the undertaking or scheme was not commenced within 10 years of acquisition. Section CB 13 does not apply because the development work does not meet the significant expenditure threshold.

Despite the fact neither s CB 12 nor s CB 13 applies, because the undertaking or scheme is one that involves the development of land or the division of land into lots, s CB 3 cannot apply. This is because of the interpretive presumption that specific provisions override general provisions (ss CB 12 and CB 13 being specific provisions relating to undertakings or schemes involving land development or division, and s CB 3 being a general provision relating to undertakings or schemes).

Example | Taura 4 – Specific land sale rule applies; section CB 3 can also apply in the alternative

Sam owns land on the outskirts of a growing town. Sam is aware a property developer is looking for a large block of land in the area for a new development. Sam acquires a neighbour's farm, with the intention of selling both blocks of land to the property developer for a profit.

Section CB 6 applies to the amount Sam derives from disposing of the land that was the neighbour's farm, as Sam acquired that land with the intention of disposing of it.

Alternatively, s CB 3 could apply to the sale of the neighbour's farm, as Sam derived an amount from a profit-making undertaking or scheme. Sam's actions are business-like and carried on with an intention to make a profit, and the amount is not derived from the mere realisation of a capital asset.

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

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References | Tohutoro

Legislative references | Tohutoro whakatureture

Income Tax Act 2007, ss CA 1, CB 3, CB 4, CB 5, CB 6, CB 11, CB 12, CB 13, CB 15, CB 16, CB 17, CB 20, CB 21 and CB 23

Case references | Tohutoro kēhi

Beetham v CIR 72 ATC 6,042 (NZSC)

Case S86 (1996) 17 NZTC 7,538 (TRA)

CIR v National Distributors Ltd (1989) 11 NZTC 6,346 (CA)

Dobson v CIR (1987) 9 NZTC 6,025 (HC)

Duff v CIR (1982) 5 NZTC 61,131 (CA)

Eunson v CIR [1963] NZLR 278 (SC)

FCT v Whitfords Beach Pty Ltd [1982] HCA 8

Grieve v CIR (1984) 6 NZTC 61,682 (CA)

Lowe v CIR (1981) 5 NZTC 61,006 (CA)

McClelland v FCT 70 ATC 4,115 (PC)

TRA 009/20 [2021] NZTRA 4

About this document | Mō tēnei tuhinga

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