

GST treatment of fees paid in relation to managed funds

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This interpretation statement considers the GST treatment of fees received by a manager of a managed fund and fees received by third-party suppliers (including investment managers) for supplies made to the manager of a managed fund.

All legislative references are to the Goods and Services Tax Act 1985 unless otherwise stated.

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Summary | Whakarāpopoto

1. Managed investment funds are an important element of the savings of New Zealanders. Money is pooled and managed by a fund manager, and a fund supervisor scrutinises the manager’s performance. The fund supervisor or a custodian holds the funds invested. Investment decisions are made by the fund manager or outsourced to an investment manager. The administration of certain aspects of the fund may also be outsourced.
2. From a GST perspective, the various relationships between the parties and the fund gives rise to interpretive issues, in particular relating to the application or non-application of the section 14(1)(a) exemption for supplies of financial services.

3. This interpretation statement addresses three key issues concerning the GST treatment of managed funds; namely, the GST treatment of:
 - fees payable by investors/the fund to the manager of a managed fund for the various services the manager supplies to the investors/the fund;
 - outsourced administrative services a third party provides to the manager of a managed fund (including services such as registry services, fund accounting, the management of financial transactions between a member and the scheme, and the management of portfolio investment entity (PIE) tax obligations); and
 - outsourced investment management services a third party provides under a contract with the manager of a managed fund.
4. This interpretation statement concludes the following.

Fees payable to the manager of a managed fund

- The fees payable to the manager of a managed fund for services supplied to the investors/the fund (or the supervisor on the investors' behalf) are not subject to GST as they are consideration for exempt supplies of financial services under section 14(1)(a). The supply or supplies made by the manager are exempt from GST as:
 - each activity the manager carries on is one of the activities listed in the definition of "financial services" (section 3); or
 - some of the activities the manager carries on are listed in the definition of "financial services" and any other services the manager supplies are reasonably incidental and necessary to the financial services the manager is supplying.

GST treatment of outsourced services in relation to a managed fund

- The outsourced supply of administrative services (including registry services, fund accounting and unit pricing) by a third party under a contract with the manager of the managed fund is a taxable supply. Administrative services are not exempt supplies of financial services because they are not one of the activities listed in section 3(1) and, generally, are not reasonably incidental and necessary to a supply of financial services.
- The supply of investment management services carried out by a third-party investment manager is either an exempt supply of financial services or a taxable supply of advice, depending on the terms of the investment manager's appointment and the manner in which this appointment is exercised and supervised.

- Where a third-party investment manager has authority to make and implement investment decisions, the investment manager makes an exempt supply of financial services because they arrange the transfer of securities (section 3(1)(l)).
- Where a third-party investment manager's investment recommendations are subject to a high level of oversight and scrutiny and a manager can veto the recommendations on the merits, the investment manager does not have authority to implement the recommendations, so such an investment manager provides investment advice, which is a taxable supply.
- However, where a manager has the right to veto an investment decision made by a third-party investment manager, the service may still be an exempt supply of arranging financial services. This would be the case where a third-party investment manager has authority to give instructions to a supervisor for the acquisition or sale of securities, and a manager's discretion to veto transactions is limited to checking that investment decisions made by the investment manager comply with the mandate. In this situation, the investment manager arranges financial services under section 3(1)(l).
- For arrangements where the manager and supervisor of the managed fund have a wider legal power to override the investment decisions of an investment manager, a court is likely to consider evidence of how an investment manager's contract is given effect to in practice. Evidence that investment decisions of an investment manager are not closely scrutinised by the manager, and transactions are largely made without any intervention by the manager or supervisor, would support a finding that the investment manager is supplying an arranging service (which would be an exempt supply).

Introduction | Whakataki

5. A "managed investment scheme" (defined in section 9 of the Financial Markets Conduct Act 2013 (FMCA)), which is generally established by a trust deed, pools money from multiple investors and then invests the pooled money according to the particular investment strategies of each managed fund (or investment fund) under the scheme. In other words, a scheme may have multiple funds. Among other classifications, a fund can be a wholesale fund, catering to wholesale investors and retail funds, or a retail fund, catering to retail investors.
6. The investors rely on the expertise of the scheme's manager (or an outsourced third-party investment manager) and the economies of scale created by pooling funds to create a larger investment.
7. The specific funds under the scheme can be created by the manager with the consent of the scheme's supervisor to segregate investor money into separate investing

strategies. A fund's assets and liabilities are legally and practically separated from those of other funds under the scheme. The specific method of separation depends on the terms of the relevant trust deed.

8. The next part of this item discusses the roles and functions of the main participants in the managed funds area. It is worth briefly summarising the arrangement involved in a managed fund.

Key features of a managed fund

9. The main participants are as follows:
 - The **investors** invest their money into a scheme or fund.
 - The **supervisor or trustee** holds the fund's assets, represents the investors' interests and monitors the fund manager's performance. The supervisor may contract out the holding of the fund's property to a separate custodian. When a managed investment scheme is to be registered (section 127 of the FMCA), it must have a licensed supervisor before registration can take place.
 - The **manager** manages the funds on the investors' behalf. This management includes administering both the fund and the fund's investment activities. The performance of either or both functions may be contracted out to a third party.
10. The managed fund is primarily regulated by the FMCA. The main documents relevant for a fund are the governing document (generally a trust deed), product disclosure statement (PDS), and statement of investment policy and objectives (SIPO).
11. The functions of the supervisor (or trustee),¹ for a retail scheme and any fund under the scheme, include:²
 - acting on investors' behalf in relation to the manager, the governing document, the terms of any offer, and any contravention of issuer obligations or applicable laws;
 - supervising the manager's performance in respect of their functions and compliance with their issuer obligations; and
 - holding the scheme property or ensuring the property is held by a custodian³ by entering into an agreement for the supply of custodial services with a third-party custodian.

¹ If the scheme is established under a trust deed, the supervisor is the trustee of the trust (section 153(4) of the FMCA). This statement does not cover the GST treatment of the supervisor/trustee.

² Section 152 of the FMCA.

³ This statement does not cover the GST treatment of a custodian.

12. The manager is responsible for the management and administration of the scheme, including any fund under the scheme.⁴ The manager's functions include:⁵
- managing the scheme property and investments, including receiving and distributing income from investments, making investment decisions, and exercising any voting rights attached to securities the scheme holds (in accordance with the SIPO and/or investment mandate for the scheme);
 - offering, issuing and redeeming the units in the scheme; and
 - administering the scheme (for example, maintaining a register of unitholders, record-keeping and reporting, and tax and regulatory compliance).
13. The manager may contract with third parties to provide some or all of its management and administration functions.⁶ For example, the manager may engage third parties to provide:⁷
- registry services, including records of unitholder details and details of their holdings in the scheme;
 - accounting services, including unit pricing and calculating the value of member interests;
 - the management of financial transactions between members and the scheme, and the management of PIE tax obligations; and
 - investment management or advisory services (that is, the management of the fund's investments or advising on what those investments should be).
14. If the manager engages a third party to provide investment management or advisory services, the nature of the services provided could take several forms. For example, a third party could be engaged to:
- provide only investment advisory services, meaning they advise on what investment decisions they think should be made regarding the investment portfolio, and the manager is then free to determine whether and to what extent to act on the advice; or

⁴ The scheme and the manager are separate persons for GST purposes.

⁵ Section 142 of the FMCA.

⁶ Section 146 of the FMCA. If the manager contracts out the performance of any of its functions, that does not affect the liability of the manager for the performance of those functions (section 146(2)(b)).

⁷ Where custodial services are contracted out, it is the supervisor rather than the manager who contracts with the custodian. The supervisor can also engage an expert (for example, an auditor, investigating accountant, valuer or actuary) if required to determine the financial position or review the business, operation, management systems, or governance of the manager or the scheme (section 155 of the FMCA).

- manage some or all of the portfolio with autonomy to make investment decisions and to give instructions to brokers to give effect to those decisions (subject to the requirements of the SIPO or investment mandate for the scheme and/or funds).
15. A manager may decide to invest all or part of the scheme property in a wholesale scheme that has its own manager. This is not, in legal terms, engaging a third party to provide investment management services, and the units in the wholesale scheme are treated like any other security the scheme holds. However, in commercial terms such an arrangement may have the same effect as engaging a third party to manage investments.
16. When the manager makes investment decisions to buy or sell securities for the scheme (including for any particular fund), the manager gives instructions to:⁸
- the supervisor or custodian to place the buy or sell orders with a broker and to settle the transaction; or
 - a broker to place the buy or sell orders and instructs the supervisor or custodian to settle the transaction.
17. To settle the transaction, the supervisor or custodian must, for a sale, arrange the transfer of the securities to the purchaser and receive the sale price and must, for a purchase, provide the funds to the vendor and take ownership of the securities.
18. The manager's investment decisions and/or execution of instructions must also comply with the requirements of the SIPO and investment mandates for the scheme and/or funds.
19. When the manager has engaged a third-party investment manager with authority to make and implement investment decisions, that third party:
- gives instructions to a broker to place the buy or sell orders; and
 - instructs the supervisor or custodian to settle the transaction.
20. For a third-party investment manager (as when the manager undertakes such activity), the investment decisions and/or execution of instructions must also comply with the requirements of the SIPO and investment mandates for the scheme and/or funds.
21. In certain circumstances, the manager or supervisor may refuse to allow a transaction initiated by a third-party investment manager to proceed, even after the third party has given instructions to a broker. In the case of the supervisor, that right of refusal is

⁸ The manager's powers in this regard may be subject to the provisions of the trust deed or other governing document or to any separate agreement(s) between the supervisor and the manager.

limited to the circumstances referred to in section 160(1) of the FMCA.⁹ In the case of the manager, the circumstances may be broader and may depend on the nature of the arrangement with the third-party investment manager.

22. The governing document (generally the trust deed) must provide for the fees and expenses that can be paid out of scheme property to any manager, third-party investment manager or administration manager, supervisor or custodian and the basis on which those fees and expenses are to be determined.¹⁰ Nevertheless, in general (and noting that such fees and expenses may be paid out of particular funds to the extent applicable), the following is the case:

- The manager is generally entitled to charge a management fee for the services they perform, which is paid out of scheme property. This is typically calculated by reference to the value of the scheme, which is referred to in the industry as the funds under management. There may also be a performance component to the manager's fee. Some schemes also provide for a transaction fee to be payable to the manager on the subscription or redemption of units. In addition, schemes may allow for an administration or membership fee to be charged to investors.
- The manager may be entitled to be reimbursed out of scheme property for expenses incurred in the performance of their functions. The supervisor may likewise be entitled to be reimbursed.
- The supervisor is paid a fee for their role as supervisor of the scheme. Depending on the terms of the governing document, this fee could be paid directly out of scheme property or by the manager, who may or may not be entitled to reimbursement for these expenses.
- Where the manager contracts with a third party to provide some or all of its management and administration functions, the manager agrees to pay a fee to the third party for those services. If the manager is entitled to be reimbursed out of scheme property for these fees, the manager may arrange for the third parties to be paid directly from the scheme by way of payment direction rather than the manager paying the third party and then getting reimbursed from the scheme.
- Where the supervisor contracts with a third-party custodian to provide custodial services, the supervisor agrees to pay a fee for those services. If the supervisor is entitled to be reimbursed out of scheme property for these fees, the supervisor may arrange for the third party to be paid directly from the scheme by way of

⁹ Namely, if the supervisor considers that the proposed acquisition or disposal would be in breach of the scheme's governing document, any rule of law or any enactment or manifestly not in the interests of scheme participants.

¹⁰ Section 135(f) of the FMCA.

payment direction rather than the supervisor paying the third-party custodian and then getting reimbursed from the scheme.

23. This interpretation statement applies to managed funds that invest in debt, equity, and participatory securities. It does not apply to investment funds where the manager of the fund directly holds real property such as commercial property or infrastructure assets. It also does not apply to venture capital funds where the manager of the venture capital fund is able to influence the management of the business of the entity it holds a stake in (which is covered by section 3(1)(m)).

Analysis | Tātari

24. Bearing in mind the statutory and factual context discussed above, this interpretation statement now considers how the GST legislation applies in relation to the three issues described at [3].

Issue one | Take tuatahi - GST treatment of fees payable to manager of a managed fund

25. Determining the GST treatment of fees paid to a managed fund manager requires consideration of the legal arrangements entered into by the parties. (See *CIR v NZ Refining Company Ltd* (1997) 18 NZTC 13,187 (CA), *Chatham Islands Enterprise Trust v CIR* (1999) 19 NZTC 15,075 (CA), and *CIR v Gulf Harbour Development Ltd* (2004) 21 NZTC 18,915 (CA).)
26. The terms of the agreement between the manager and investors are in the governing document (generally a trust deed) and the PDS. As a trust deed for a managed fund has no effect if it contravenes or is inconsistent with the FMCA, the manager's obligations under a trust deed must be consistent with the manager's statutory obligations under the FMCA (section 138).
27. The manager's responsibilities were discussed at [12]. These responsibilities include:¹¹
- managing the scheme property and investments, including receiving and distributing income from investments, making investment decisions, and exercising any voting rights attached to securities held by the scheme (in accordance with the SIPO and/or investment mandate for the scheme);
 - offering, issuing and redeeming the units in the scheme; and
 - administering the scheme (for example, maintaining a register of unitholders, record-keeping and reporting, and tax and regulatory compliance).

¹¹ Section 142 of the FMCA.

28. The manager does not supply marketing and advertising services, compliance services or tax advice. Investors do not contract for the supply of these services. The manager carries out marketing and advertising for the purpose of promoting and enabling the issue of units to investors, but it does not supply those services to anyone, they are internal activities that support their actual supplies. The manager complies with their obligations under the FMCA to enable them to issue or transfer units and to continue to act as the manager of a managed fund.

Supplies of financial services are exempt supplies

29. Section 14(1)(a) exempts the supply of financial services, stating:

14 Exempt supplies

- (1) The following supplies of goods and services shall be exempt from tax:
- (a) the supply of any financial services (together with the supply of any other goods and services, supplied by the supplier of those financial services, which are reasonably incidental and necessary to that supply of financial services), not being a supply referred to in subsection (1B):

30. As set out in section 14(1)(a), the supply of “other goods and services” is also an exempt supply if the:
- other goods and services are supplied by the supplier of financial services together with the supply of the financial services; and
 - supply of the other goods and services is “reasonably incidental and necessary” to the supply of those financial services.
31. A “financial service” is any one or more of the activities listed in the definition in section 3(1). The relevant paragraphs of that definition for the purposes of this interpretation statement are as follows:

3 Meaning of term financial services

- (1) For the purposes of this Act, the term **financial services** means any 1 or more of the following activities:
- ...
- (c) the issue, allotment, drawing, acceptance, endorsement, or transfer of ownership of a debt security:
- (d) the issue, allotment, or transfer of ownership of an equity security or a participatory security:
- ...

- (ka) the payment or collection of any amount of interest, principal, dividend, or other amount whatever in respect of any debt security, equity security, participatory security, credit contract, contract of life insurance, retirement scheme, financial option, or futures contract:
- (l) agreeing to do, or arranging, any of the activities specified in paragraphs (a) to (ka), other than advising thereon:
- ...

Issue and redemption of units

32. The issue, allotment or transfer of ownership of a participatory security is a financial service (section 3(1)(d)). “Participatory security” is defined in section 3(2) as follows:

participatory security means any interest or right to participate in any capital, assets, earnings, or other property of any person where that interest or right forms part of a contributory scheme; and includes an interest in a unit trust (within the meaning of section YA 1 of the Income Tax Act 2007); but does not include an equity security, a debt security, money, or a cheque

33. “Contributory scheme” is also defined in section 3(2) as follows:

contributory scheme—

- (a) means any scheme or arrangement that, in substance and irrespective of the form of the scheme or arrangement, involves the investment of money where—
 - (i) the investor acquires or may acquire an interest in or right in respect of property; and
 - (ii) that interest or right will or may be, under the terms of investment, used or exercised in conjunction with any other interest in or right in respect of property acquired in similar circumstances, whether at the same time or not; but
- (b) does not include a scheme or arrangement described in paragraph (a) that has 5 or fewer investors, provided that neither the manager of the scheme nor any associated person of the manager is the manager of another such scheme or arrangement

34. An interest in a unit trust (as defined in section YA 1 of the Income Tax Act 2007¹²) is also included in the definition of participatory security (section 3(2)).

¹² Section YA 1 of the Income Tax Act 2007 defines “unit trust” as follows:

35. An interest in a managed fund would satisfy the definition of “participatory security”. Therefore, fees payable to the manager for the issue, redemption or repurchase of interests in a managed fund are not subject to GST as the fees are consideration for a financial service under section 3(1)(d). As such they are consideration for an exempt supply.

Payments in respect of units and securities

36. The payment or collection of any amount in respect of a debt security, equity security or participatory security (or arranging the payment or collection of such amounts) is a financial service (section 3(1)(ka) and (l)).
37. A managed fund may invest in debt securities, equity securities or participatory securities, including investing in another managed fund. The manager collects and distributes amounts in respect of securities (or arranges these activities). These activities are financial services under section 3(1)(ka) and (l).
38. Therefore, the fees relating to these activities are not subject to GST as they are consideration for an exempt supply.

Investment activities of the manager

39. Arranging the transfer of debt securities, equity securities or participatory securities is a financial service, but advising on the transfer of such securities is not a financial service (section 3(1)(c), (d) and (l)).

unit trust—

- (a) means a scheme or arrangement that is made for the purpose or has the effect of providing facilities for subscribers, purchasers, or contributors to participate, as beneficiaries under a trust, in income and capital gains arising from the property that is subject to the trust; and
- (b) does not include—
- (i) a trust for the benefit of debenture holders:
 - (ii) the Common Fund of Public Trust:
 - (iii) a group investment fund established by Public Trust:
 - (iv) the Common Fund of the Maori Trustee:
 - (v) a group investment fund established under the Trustee Companies Act 1967:
 - (vi) a friendly society registered under the Friendly Societies and Credit Unions Act 1982:
 - (vii) a superannuation fund:
 - (viii) an exempt ESS:
 - (ix) a fund that meets the requirements of section CW 45 (funeral trusts):
 - (x) any other trust of any specified kind that is declared not to be a unit trust for the purposes of section HD 13 (unit trusts) by the Governor-General by Order in Council (and such an order is secondary legislation (see Part 3 of the Legislation Act 2019 for publication requirements)).

40. The manager is responsible for investing the fund's property in accordance with the SIPO and investment mandate and objectives specified in the trust deed or agreed with the trustee. The manager has discretion (subject to the SIPO and investment mandate) to make and implement decisions on what, and when, securities should be bought or sold with investor funds.

Manager does not provide advice

41. The manager does not provide advice on the transfer of securities. To advise means to recommend or inform, counsel or give an opinion (*Concise Oxford Dictionary* (12th ed, Oxford University Press, 2011), and *J R Moodie Co Ltd v MNR* [1950] 2 DLR 145 at 148 (SCC)). The manager does not give recommendations, counsel, or opinions on securities transactions. The manager has discretion, subject to the fund's investment policy and objectives, to make and implement investment decisions. The supervisor, who represents investors, must comply with the manager's instructions to buy or sell securities unless a transaction would be in breach of the scheme's governing document, any rule of law, or any enactment, or is manifestly not in the interests of the scheme participants (section 160 of the FMCA).

Manager's investment activities constitute an arranging service

42. "Arrange" means "cause to occur", "plan or provide for" or "give instructions for" (*Databank Systems Ltd v CIR* (1987) 9 NZTC 6,213 (HC), *Royal Bank of Canada v R* (2005) TCC 802, and *Canadian Medical Protective Assn v R* [2009] FCA 115). More than one person could be involved in arranging a financial service (*Canadian Medical Protective Assn*).
43. The manager carries out research and market analysis for the purpose of making investment decisions. Considered in isolation, research and market analysis are not financial services. However, the arranging of a supply of financial services could include activities that considered in isolation are not financial services. If a sufficient causal link exists between the research and market analysis activities and the transfer of securities, the research and market analysis is part of an arranging service.
44. To determine whether services constitute the arranging of financial services it is necessary to consider whether a sufficient relationship exists between the services and the supply of financial services. To be the arranging of the transfer of securities, a sufficient relationship must exist between the manager's activities and the transfer of securities.

45. Two Canadian cases provide some assistance in applying the “arranging” test in an investment management context.¹³ These cases are helpful both for the issue of whether a manager’s investment activities are exempt supplies of financial services and for the issue of whether an outsourced investment manager’s activities are exempt supplies of financial services (discussed from [84]).
46. In *General Motors of Canada Ltd v R*,¹⁴ the investment managers issued buy and sell orders to brokers to complete financial transactions. The trustee reviewed each order and provided funds to the broker to do the deal.¹⁵ The trustee was not obliged to complete the transaction,¹⁶ and in addition the fund’s administrator could veto investment decisions the investment manager made. Notably, the investment management agreement stated the investment managers are “to provide investment advice and other related services”.¹⁷ Campbell J held:¹⁸

The evidence as a whole points conclusively to the fact that the Investment Managers, in reality, did not exercise exclusive authority over the investment choices, and did not possess access to the funds to permit the “arranging for” transfers of financial instruments. Given that no less than two additional parties, the Trustee and GMCL, could veto the execution of the buy/sell orders, and the fact that the Investment Managers did not have access to the funds, support my determination, on a balance of probabilities, that the Investment Managers did not possess the authority nor the means to “arrange for” the transfer of financial instruments for GMCL.

47. Campbell J held further that the “arranging for a service” aspect was confined to calling a broker to complete the trade.¹⁹
48. Clearly, Campbell J considered it was relevant that two parties could veto the execution of the buy and sell orders. This factor is relevant, but it is not on its own decisive. That factor needs to be taken into consideration with all other relevant factors to decide whether a sufficient relationship exists between the services and the supply of financial services.
49. In *Canadian Medical Protective Assn*, the third-party investment manager had an unfettered discretion to buy and sell a particular group of securities. The Federal Court

¹³ These Canadian cases are useful in a New Zealand financial services context because the relevant parts of the definition of financial services considered in the cases are essentially the same as the definition in New Zealand’s GST Act.

¹⁴ *General Motors of Canada Ltd v R* [2008] TCC 117 (Tax Court of Canada). Although *General Motors* (TCC) was upheld on appeal in *General Motors of Canada Ltd v R* [2009] FCA 114, the decision that the third-party investment manager did not supply an exempt financial service was not decided on appeal.

¹⁵ At [93].

¹⁶ At [98].

¹⁷ At [99].

¹⁸ At [99].

¹⁹ At [100].

of Appeal referred to dictionary meanings of “arranging for”; namely, “cause to occur”, “give instructions”, “make preparation for” and “plan”.²⁰ The court found that the words “give instructions” and “make preparation for” are acceptable interpretations of the words “arranging for” and are as wide and elastic as one wishes them to be.²¹

50. The Court held the dominant character of the service supplied was the research and analysis aspect of the trade but considered as a whole the services the investment managers performed, including the final order to buy or sell or the decision to hold, could not be divided.²² Further, the manager did not provide advice, since there was no one to provide advice to except themselves.²³ The Court went on to hold that the result of the fund manager’s service was to “cause to occur a transfer of ownership ... of a financial instrument”.²⁴ As a result, the services provided were “arranging” and exempt.²⁵ Paragraphs 62 to 64 of the judgment are set out below:

[62] On the one hand, there is the world of a difference between the services of the investment managers and those of a broker who generally accomplishes a more mechanical type of work. If I were to retain the dominant character of the investment managers’ services, the research and analysis aspect of the trade would be the dominant character of the services they supply.

[63] On the other hand, the research and analysis aspect of the trade will be purposeless if it does not end with a buy or sell order or a “hold” decision. The final order is an essential characteristic of the management of the funds by the investment manager. Otherwise, the investment manager does not manage at all.

[64] I find that, considered as a whole, the services performed by investment managers cannot be divided. It is a mix. They do not provide advice, since there is no one to provide advice to except themselves. The end result of their services is to “cause to occur a transfer of ownership ... of a financial instrument”. They fall within paragraph 123 (1) (d) and (l) of the Act.

51. Although *Canadian Medical Protective Assn* is not binding on a New Zealand court, the relevant parts of the definition of financial services considered in that case and the definition in the New Zealand GST Act are essentially the same. The Court held that the investment manager’s services were financial services (the arranging of the transfer of financial instruments).
52. The Commissioner considers that the approach applied in these cases is consistent with the approach a New Zealand court would apply to determine the true and substantial nature of the consideration provided to the recipient (the supply contracted for). This is considered objectively from the customer’s perspective – in this case, a

²⁰ At [60].

²¹ At [61].

²² At [62]–[64].

²³ At [64].

²⁴ At [64].

²⁵ At [66].

typical investor or the fund (*Auckland Institute of Studies Ltd v CIR* (2002) 20 NZTC 17,685 (HC)).

53. The degree of knowledge and skill with which a service is supplied is relevant to the quality of the service but does not determine the nature of the service.
54. Research and market analysis for the purpose of making investment decisions are important elements in the service provided to investors in a fund. However, a typical investor in a managed fund does not seek research and market analysis as ends in themselves. The purpose of a managed fund is to provide facilities for investors to participate as beneficiaries in the income and capital arising from the trust property. Investors acquire interests in a managed fund to obtain an interest in the trust's assets. Research and market analysis are carried out to establish the pool of securities in which investors have an interest as beneficiaries. Research and market analysis for the purpose of making investment decisions and implementing those decisions are inextricably linked.
55. In some cases, research and analysis may not lead to the transfer of securities. However, this would not alter the nature of the supply. When investors pay money to the manager for investment, they decide that securities the manager selects will be acquired or sold for their benefit. The manager's research and analysis activities are carried on to give effect to the investors' decision. The same process is carried out by the manager in deciding whether to buy, sell or hold securities. Research and analysis are not carried out as ends in themselves, but as part of the process by which the manager arranges for securities to be bought or sold.
56. The manager is directly involved in the process by which securities are bought or sold for the investors' benefit. As the manager has discretion to make investment decisions and the supervisor must comply with the manager's instructions (subject to any powers the supervisor may have in this regard), a direct relationship exists between the manager's research and analysis activities and the transfer of securities. The manager does not merely facilitate or enable the transfer of securities by or to the supervisor. As the manager causes the transfer of securities to occur, plans and provides for the transfer of securities, and gives instructions for the transfer of securities, the manager's investment management activities constitute arranging for the transfer of securities.
57. Therefore, the manager's activities relating to the investment of the trust property are financial services under section 3(1)(l), being arranging the supply of a financial service (the transfer of ownership of securities), so are exempt supplies of financial services.

Administration activities

58. The manager's administration activities (including services such as registry services, fund accounting, the management of financial transactions between a member and the

scheme, and the management of PIE tax obligations) are not any of the activities listed in section 3(1). Therefore, these activities are not financial services. However, the supply of administrative services is an exempt supply (by virtue of section 14(1)(a)) if the services are:

- supplied by the manager; and
- reasonably incidental and necessary to the supply of financial services by the manager.

59. For section 14(1)(a) to apply to the supply of goods and services other than the supply of financial services:

- the goods and services must be supplied by a person who supplies the financial services;
- the supply of the goods and services must be reasonably incidental to the supply of financial services. This requires that the supply of the other goods and services must occur in conjunction with the supply of financial services;
- the supply of the other goods and services must be subordinate to the supply of financial services²⁶; and
- the supply of the goods and services must be reasonably necessary to the supply of financial services. To be “reasonably necessary” to the supply of financial services, it would not be sufficient that the supply of other goods and services are merely desirable to the supply of financial services. There must be a degree of need for the supply of other goods and services to be supplied with financial services, but the supply of other goods and services need not be essential or absolutely necessary to the supply of financial services (in the sense that the financial services could not be supplied without the other goods and services being supplied)²⁷.

60. To summarise, a supply of non-financial services by the manager is reasonably incidental to the supply of the financial services by the manager if the supply occurs in conjunction with the supply of those financial services **and** is subordinate to the supply of the financial services. To be “reasonably necessary” to the supply of financial services by the manager, it is not enough that the administration services are merely

²⁶ *Department of Health and Social Security v Envoy Farmers Ltd* [1976] 2 All ER 173; *Canadian National Railway Co v Harris* [1946] SCR 352; *CH Beazer (Holdings) plc v C & E Commrs* (1987) 3 BVC 623; *Mindell v Canadian Northern Shield Insurance Co v Mindell* [1990] BCJ No 15; *State of Victoria v Commonwealth* [1975] 7 ALR 277; *R v Sundown* [1999] 1 SCR 393; *Doom v Commissioners of Customs & Excise* (1973) VATTR 61).

²⁷ *See R v Shayler* [2002] 2 All ER 477; *Re an Inquiry under the Company Securities (Insider Dealing) Act 1985* [1988] 1 All ER 203; *Re H-L (A child)* [2013] EWCA Civ 655; *M v The Queen* (Court of Appeal CA 819/2011; 5 April 2012); *Elcham v Commissioner of Police* [2001] NSWSC 614; *Aiken v Shaw* (1933) SLT 21.

desirable to the supply of the financial services. However, the other goods and services need not be essential or absolutely necessary to the supply of financial services (in the sense that the financial services could not be supplied without the other goods and services).

61. Fund accounting and unit pricing are reasonably incidental and necessary to the supply of financial services by the manager. Fund accounting and unit pricing are subordinate to the issue or redemption of units and are necessary to establish the price at which units are to be issued or redeemed by the manager.
62. The maintenance of a registry is also reasonably incidental and necessary to the supply of financial services. A register of members is maintained because proper records must be kept to enable the persons for whom the scheme property is held (and the extent of their interest in the scheme property) to be identified.
63. The manager must provide reports to investors because the manager receives funds from investors and must account for these funds. These reporting activities are reasonably incidental and necessary to the supply of financial services by the manager.
64. Therefore, the supply by the fund manager of services in relation to the administration of a managed fund is an exempt supply under section 14(1)(a). This is illustrated in Example | Taura 1.

Example | Taura 1 – Manager providing administration services to the managed fund

Company A is the manager of a managed fund. Company A undertakes all the administration of the managed fund (such as registry services, record-keeping and reporting, tax and regulatory compliance); offers, issues, and redeems interests in the fund; and manages the scheme property and funds (including receiving and distributing income from investments, making investment decisions and exercising voting rights).

Company A's supplies to investors in the fund and the fund itself are exempt supplies. The supplies are either supplies of financial services being activities listed in section 3(1) or are reasonably incidental and necessary to those supplies of financial services.

Accordingly, no output tax is payable on the supplies by the manager.

Manager's activities are not characterised as a supply of management services

65. An argument exists that the relevant supply for a managed fund is a single supply of management services that is not an exempt supply of financial services. A transaction involves a single supply where:
- one element in the transaction is the principal or dominant element in the supply and other elements of the transaction are incidental or ancillary to the principal supply; or
 - two or more elements (none of which is the principal or dominant supply) are so closely linked that they form objectively a single indivisible economic supply.

See *Auckland Institute of Studies Ltd, Levob Verzekeringen BV v Staatssecretaris van Financiën* [2006] STC 766 (ECJ) and [IS 18/04: Goods and services tax – single supply or multiple supplies](#).

66. Without a statutory definition of financial services, it may have been possible to argue that the supply made by the manager (considered as a whole) was a single supply of the management of a managed fund. The argument would be that the investors acquire an interest in securities selected by the manager and a right to share in the income from the securities. As each element of the transaction is necessary and integral to the supply sought and obtained by investors, all the manager's activities can be regarded as a single supply of services. The manager manages a fund in the sense that they control and direct the managed fund.
67. However, the scope of the exemption in respect of financial services is determined by the list of specific activities in section 3(1) (see *Gulf Harbour Development Ltd*).
68. As a financial service is "any one or more" of the activities listed in section 3(1), a financial service can consist of more than one of the activities in section 3(1). The legislation contains its own test of whether the supply of non-financial goods and services is part of a supply of financial services. If goods and services other than financial services are supplied by a person who supplies financial services and the supply of the non-financial goods and services is reasonably incidental and necessary to the supply of those financial services, the supply of the non-financial goods and services is part of the supply of the financial services and shares the same GST treatment (see at [58]).
69. The supply or supplies made by the manager are exempt from GST if:
- each activity the manager carries on is one of the activities listed in the definition of financial services; or

- some of the activities the manager carries on are listed in the definition of financial services and any other services supplied by the manager are reasonably incidental and necessary to the financial services supplied by the manager.

Management of a retirement scheme

70. The Commissioner acknowledges that the management of a retirement scheme is a specified financial service (section 3(1)(j)²⁸) but in contrast the “management of a managed fund” is not one of the activities listed in section 3(1). It might be argued that this suggests the activities of the manager of a managed fund were not intended to be financial services.
71. However, the manager’s activities include the specific activities listed in the definition of financial services in section 3(1) as well as services that are reasonably incidental and necessary to the supply of financial services by the manager (section 14(1)(a)). If the supplies made by the manager satisfy the specific paragraphs of section 3(1) they cannot be treated as taxable supplies on the basis of an argument that the activities of the manager (considered as a whole) comprise the management of a managed fund, and the management of a managed fund is not specified in section 3(1). The explicit reference to the management of a retirement scheme in section 3(1)(j) does not override the existence of the specific paragraphs of section 3(1) in relation to a managed fund.
72. Section 3(1)(j) applies to determine the GST treatment of services constituting the management of a retirement scheme. Retirement scheme is defined in section 3(2) by reference to the meaning of the term in section 6(1) of the FMCA. The definition of retirement scheme in section 6(1) of the FMCA includes a registered scheme that is a KiwiSaver scheme or a superannuation scheme (as also defined in the FMCA). “Management” refers to control, direction, planning, and decision-making. The management of a retirement scheme such as a KiwiSaver scheme or superannuation scheme will involve the control, direction, planning, and supervision of the scheme and making decisions in respect of the scheme.
73. Therefore, a manager of a managed fund that meets the definition of a “retirement scheme” will be providing an exempt supply in providing their services to the managed fund. On the basis of section 14(1)(a) this exemption will include any other goods and services the manager provides that are reasonably incidental or necessary to those services. This interpretation statement, however, is intended to cover the GST treatment of the services supplied by the manager of a scheme that is not a “retirement scheme²⁹”. Section 3(1)(j) has only been considered in this interpretation

²⁸ Section 3(1)(j) includes in the term financial services “the provision, or transfer of ownership, of an interest in a retirement scheme, or the management of a retirement scheme”.

²⁹ “Restricted schemes” as defined in section 6 of the FMCA are also not covered by this statement as they are retirement schemes.

statement because of the argument that an absence of a similar provision for non-retirement schemes means that the management of such schemes does not involve financial services.

Issue two | Take tuarua - GST treatment of outsourced services in relation to a managed fund

74. The manager of a managed fund may enter into a contract with a third party under which the third party agrees to carry out some of the functions the manager is required to perform for the fund and investors.
75. The supplier of services is the person who is contractually obliged to supply the services, and the recipient is the person who can enforce the performance of the services (*Wilson & Horton Ltd v CIR* (1995) 17 NZTC 12,325 (CA) and *CIR v Capital Enterprises Ltd* (2002) 20 NZTC 17,511 (HC)). The manager of a managed fund supplies services to the fund on behalf of the investors. The contracting out of the services does not relieve the manager of their contractual obligations or statutory obligations to provide the services to the fund (*Tolhurst v Associated Portland Cement Manufacturers (1900) Ltd* [1902] 2 KB 660 (CA) and *Savvy Vineyards 3552 Ltd v Kakara Estate Ltd* [2015] 1 NZLR 281 (SC)).
76. Where the manager enters into a contract with a third party for the supply of any services that the manager is required to supply under its contract with the fund, there will be a:
- supply of the services by the manager to the fund; and
 - a separate supply of equivalent services by the third party to the manager.
77. This part of the interpretation statement considers services provided for a managed fund that are supplied by a third party under a contract with the manager. The manager may contract out their administrative functions (including services such as registry services, fund accounting, the management of financial transactions between a member and the scheme, and the management of PIE tax obligations). The manager may also contract out investment management by appointing an investment manager to manage all or some of the assets of a managed fund.

Outsourced services are not necessarily exempt supplies

78. Outsourced services are not exempt supplies merely because the services are acquired and used by the manager to make exempt supplies to investors (*CIR v Databank Systems Ltd* (1990) 12 NZTC 7,227 (PC)).
79. To be a financial service, an outsourced service must be one of the activities listed in section 3(1) in relation to the supplier (the third party) and the recipient (the manager).
-

80. As noted above, for the supply of goods and services other than the supply of a financial service to be an exempt supply, the:
- goods and services must be supplied by a supplier of financial services together with the supply of financial services; and
 - supply of the goods and services must be “reasonably incidental and necessary” to the supply of those financial services (section 14(1)(a)).
81. If an outsourced service is not a financial service, the supply of the service is not an exempt supply. This is because the service is not supplied by a person who supplies financial services.
82. If any service supplied by a third party to the manager of a managed fund is a taxable supply, the manager is not likely to be entitled to an input tax deduction for those supplies. This is because the services are generally acquired by the manager for the purpose of making their exempt supplies.

Administrative services

83. The various administrative obligations of a manager that could be outsourced to a third party under a contract with the manager (such as the maintenance of a register of unitholders and the accounting functions performed by a third party) are not financial services because they are not one of the activities listed in section 3(1). (But see below at [90] for the situation where administrative services and investment management services and/or other services are outsourced to the same person.) The recording of the effect of agreements or arrangements made by the manager is not an arranging service and is not a financial service under section 3(1)(l) (*Databank* (PC) at 7,231). This is illustrated in Example | Tauria 2.

Example | Tauria 2 – Outsourced administrative services

Company B enters into a contract with a manager of a managed fund. Company B agrees to:

- keep and maintain a register of investors;
- keep records of subscriptions, units held by investors, unit prices, income entitlements and other matters that must be recorded in terms of the trust deed or any relevant legislation; and
- provide information to the manager to enable the manager to comply with the manager’s statutory and contractual obligations.

As maintaining records and providing information are not any of the activities listed in the definition of financial services, the services supplied to the manager are not

financial services. They also do not come within section 14(1)(a) as being the supply of other goods and services, supplied by the supplier of financial services, that are reasonably incidental and necessary to that supply of financial services. The supply of the services enables the manager to supply financial services to investors. However, the services are not part of the supply of financial services by the manager as they are supplied by a different person. Therefore, the supply of the services is not an exempt supply under section 14(1)(a) and is a taxable supply.

As these services are generally acquired by the manager for the purpose of supplying exempt supplies of financial services, the manager is not likely to be entitled to an input tax deduction.

Investment management

84. Arranging for the transfer of debt securities, equity securities or participatory securities is a financial service, but advising on the transfer of securities is not a financial service (section 3(1)(c), (d) and (l)). The meanings of “advise” and “arrange” were first discussed at [41] and [42] and are further discussed in the following paragraphs.
85. An investment manager’s activities involve arranging the transfer of securities if a sufficient causal link exists between the activities and the transfer of securities. This is the case where an investment manager has full authority to both make and carry out investment decisions. However, the investment manager is not supplying an arranging service where the manager does not need to accept recommendations made by an investment manager, and the investment manager does not have authority to give instructions to the supervisor or custodian (who holds the assets of the managed fund) for the acquisition or sale of securities. In these circumstances, the essential nature of the services provided by an investment manager is the provision of advice, which is a taxable supply (see *General Motors of Canada Ltd* and *Canadian Medical Protective Assn* (discussed from [46])). The following paragraphs consider this distinction in more detail.
86. The supply of investment management carried out by a third-party investment manager is either an exempt supply of financial services or a taxable supply of advice, depending on the terms of the appointment of the third-party investment manager and the manner in which this appointment is exercised and supervised. Where an investment manager has authority to make and implement investment decisions, the investment manager makes an exempt supply of financial services because they arrange the transfer of securities (section 3(1)(l)).
87. Where an investment manager’s investment recommendations are subject to a high level of oversight and scrutiny and a manager can veto the recommendations on the merits, the investment manager does not have authority to implement investment

recommendations, so such an investment manager provides investment advice, which is a taxable supply. This is illustrated in Example | Taura 3.

Example | Taura 3 – Outsourced investment management services that are not “arranging” services

The manager of a managed fund enters into an agreement with an investment manager, Company C. Company C’s obligations are to recommend investment decisions in accordance with investment guidelines agreed with the managed fund manager. Company C has no authority to give instructions to the supervisor who holds the assets of the fund to buy or sell securities or to complete settlement of securities transactions. The supervisor is not required to comply with the instructions of Company C and the transfer of securities cannot occur without the managed fund manager’s approval. Notwithstanding that, the recommendations are routinely accepted by the manager and implemented for the managed fund.

Arranging the transfer of debt securities, equity securities or participatory securities is a financial service (section 3(1)(c), (d) and (l)). To be arranging the transfer of securities, a sufficient relationship must exist between the investment manager’s services and a transfer of securities. As securities will be bought or sold only if the managed fund manager instructs the supervisor to do so, Company C’s activities do not constitute arranging the transfer of securities. The service supplied by Company C is advising on the transfer of securities, which is specifically excluded from the definition of financial services. Therefore, Company C’s services are a taxable supply.

As Company C’s services are generally acquired by the manager for the purpose of supplying financial services, the manager is not likely to be entitled to an input tax deduction on Company C’s services.

88. However, in some circumstances where a manager has the right to veto an investment decision made by a third-party investment manager, the service will still be an exempt supply of arranging financial services. This would be the case where an investment manager has authority to give instructions to a supervisor for the acquisition or sales of securities, and a manager’s discretion to veto transactions is limited to checking that investment decisions made by the investment manager comply with the mandate. In this situation, the investment manager arranges financial services under section 3(1)(l). This is illustrated in Example | Taura 4.

Example | Tauria 4 – Outsourced investment management services that are “arranging” services even where the manager and supervisor have a limited right to veto the investment manager’s decisions

The manager of a managed fund enters into an agreement with an investment manager, Company D. Company D’s obligations are to make investment decisions in accordance with investment guidelines agreed with the managed fund manager. Company D has authority to give instructions to the supervisor who holds the assets of the fund to buy or sell securities or to complete settlement of securities transactions. The manager and supervisor can intervene to countermand the instructions of Company D only where the decisions conflict with the investment mandate of the fund (or, for the supervisor, where section 160 of the FMCA applies).

Arranging the transfer of debt securities, equity securities or participatory securities is a financial service (section 3(1)(c), (d) and (l)). To be arranging the transfer of securities, a sufficient relationship must exist between Company D’s services and a transfer of securities. As securities will be bought or sold if the investment manager instructs the supervisor to do so, subject to very limited “veto” powers of the managed fund manager and the supervisor, Company D’s activities constitute arranging the transfer of securities. Therefore, it is an exempt supply of financial services.

Accordingly, no output tax is payable on the supply by Company D and there is no input tax for the managed fund manager.

Variation – outsourced investment management services that are “arranging” services even where the manager has a limited right to veto the investment manager’s decisions, and the investment manager must give prior notice of the proposed investment decisions

The facts are as above, but Company D is required to advise the manager and supervisor of the investment decisions it proposes to make. As above, the manager and supervisor are able to intervene to countermand the instructions of Company D only where the decisions conflict with the investment mandate of the fund (or, for the supervisor, where section 160 of the FMCA applies).

Company D’s activities still constitute arranging the transfer of securities. It is an exempt supply of financial services. This is even though Company D is required to advise the manager and supervisor of the proposed investment decisions ahead of time and even though there is a limited ability to not follow Company D’s decisions.

Accordingly, no output tax is payable on the supply by Company D and there is no input tax for the managed fund manager.

89. For arrangements where the manager and supervisor of the managed fund have a wider legal power to override the investment decisions of an investment manager, a court is likely to consider evidence of how an investment manager's contract is given effect to in practice. Evidence that investment decisions of an investment manager are not closely scrutinised by the manager, and transactions are largely made without any intervention by the manager or supervisor would support a finding that the investment manager is supplying an arranging service. This is illustrated in Example | Tauria 5.

Example | Tauria 5 – Outsourced investment management services that are “arranging” services where the manager has the right to not follow the investment manager’s decisions but in practice never exercises that right

The manager of a managed fund enters into an agreement with an investment manager, Company E. Company E's obligations are to make investment decisions in accordance with investment guidelines agreed with the managed fund manager. Company E has authority to give instructions to the supervisor who holds the assets of the fund to buy or sell securities or to complete settlement of securities transactions. However, the manager and supervisor have a right to intervene to countermand the instructions of Company E in circumstances where they disagree with Company E's decisions.

The longstanding practice of both the manager and supervisor is to follow the decisions of Company E, and the only real scrutiny of those decisions is to ensure they satisfy the investment mandate (and to ensure no breach of section 160 of the FMCA). The only time decisions have been countermanded was where the investment mandate was inadvertently breached.

Arranging the transfer of debt securities, equity securities or participatory securities is a financial service (section 3(1)(c), (d) and (l)). To be arranging the transfer of securities, a sufficient relationship must exist between Company E's services and a transfer of securities. In practice, securities are bought or sold if Company E instructs the supervisor to do so subject to very limited “veto” powers of the managed fund manager and the supervisor, so Company E's activities constitute arranging the transfer of securities. It is an exempt supply of financial services. This is even though the manager and supervisor have a more general power to not follow Company E's decisions (compared with Example | Tauria 4).

Accordingly, no output tax is payable on the supply by Company E and there is no input tax for the managed fund manager.

Exempt investment management and/or other financial services and administration outsourced to the same person

90. Where exempt investment management³⁰ and/or other financial services (for example, the issue and redemption of units in the fund) are outsourced, together with administrative services, it will be a question of fact whether those administrative services are “reasonably incidental and necessary” to the various exempt supplies of financial services. In some cases that may be clearly the case (for example, where the fund manager outsources all of their activities to the same third party such that the administrative services must support the financial services supplied by the third party). In other cases it may be less clear (for example, where investment management and administrative services are outsourced to the same third party, but not all the administrative services can be said to support the financial services involved with exempt investment management).
91. Each factual situation will need to be carefully scrutinised in terms of the test for reasonably incidental and necessary (see above at paragraphs 59 and 60), and it is not possible to make a broad statement in the absence of particular facts.
92. Example | Taura 6 illustrates these points.

Example | Taura 6 – A manager fully outsources services to a third party

The manager of a managed fund enters into an agreement with Company F which involves the manager outsourcing to Company F all the services the manager must provide to the fund. This includes investment management (of a type that means Company F is arranging the transfer of securities and not just advising), the issue and redemption of units, the collection and payment of sums in relation to securities, and all associated administrative services that the manager was responsible for.

Company F’s services of investment management (section 3(1)(l)), the issue and redemption of units (sections 3(1)(c) and (d)), and the collection or payment of amounts in respect of securities (section 3(1)(ka)) are all financial services and therefore exempt supplies.

The administrative services Company F provides are reasonably incidental and necessary to the supplies of financial services and therefore also exempt by virtue of section 14(1)(a). This is for the same reasons discussed in [61] to [64] and illustrated in Example 1. The administrative services are provided together with the financial

³⁰ Based on the discussion above about when outsourced investment management will be exempt as “arranging” or taxable as “advising”.

services and are subordinate to them and are also necessarily undertaken to make those supplies of financial services.

Variation – the manager outsources investment management and administrative services to a third party

As a variation on the above, the manager only outsources to Company F the investment management of the managed fund and all the administrative services the manager is required to undertake. These administrative services relate to all the different functions that the manager is obliged to fulfil, including the investment management.

As above, the investment management will be a financial service and an exempt supply (as Company F is arranging the transfer of securities and not just advising).

However, the administrative services Company F provides are not all reasonably incidental and necessary to its supplies of financial services (which are only the supplies of investment management) and therefore are not all exempt by virtue of section 14(1)(a).

The administrative services provided together with the investment management will be reasonably incidental and necessary to Company F's financial services of investment management, as they are subordinate to them and are also necessarily undertaken to make those supplies of financial services.

On the other hand the administrative services provided by Company F in relation to the manager's own supplies of financial services (that is, the services that were not outsourced) do not satisfy the test of being reasonably incidental and necessary to a supply of financial services made by Company F so as to satisfy section 14(1)(a).

(These conclusions (for both the first part of the example and the variation) would not change if Company F was a group company.)

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