Inland Revenue
Te Tari Taake

TECHNICAL DECISION SUMMARY > ADJUDICATION

WHAKARĀPOPOTO WHAKATAU HANGARAU > WHAKAWĀ

Sale of bare land when intended for a subdivision

Decision date | Rā o te Whakatau: 27 November 2023

Issue date | Rā Tuku: 28 March 2024

TDS 24/05

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This document is a summary of the original technical decision so it may not contain all the facts or assumptions relevant to that decision.

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Subjects | Kaupapa

Income tax: intention to sell; subdivision; sale of bare land; joint venture; partnership; identifiable capital asset.

Taxation laws | Ture tāke

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

Facts | Meka

1. This dispute involved three Taxpayers who held Units in an unincorporated joint venture (the Joint Venture) with other members.
2. On its formation, the Joint Venture acquired an undivided beneficial ownership interest in various assets including land.
3. Over a number of years following purchase, activities of the Joint Venture included subdividing and selling a number of residential sections from the land.
4. In the year of assessment, the Taxpayers sold their Units (including their underlying interests to the remaining undivided land). They each made a profit on the sale.
5. Land held by the Joint Venture at the time of the Unit sale comprised:
    - Undeveloped farmland that had received special housing area designation. This was being used for grazing while the Joint Venture was considering making resource management consent applications for residential section development.
    - Residential land that had nothing done to it as the Joint Venture did not consider it practicable for further development (used for grazing).
    - A large piece of rural zoned land that was also used for grazing.
6. The Taxpayers returned the proceeds from the sale as assessable income in their tax returns but, subsequently, issued notices of proposed adjustment to remove this amount. They contended, in relation to s CB 6, that while the intention was to sell subdivided land, the parties never intended to sell bare land. There was a long-term hope that as much of the land as possible could be subdivided and sold. This intention was formed at the time the Joint Venture came together.

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7. Given tranches of the land had previously been subdivided and sold, and proceeds returned under s CB 12 or predecessor sections, the Taxpayers contended s CB 6 could not apply to the remainder of the land.

8. The Taxpayer also argued that the sale was a sale of the Units, an identifiable capital asset, and that the land provisions could not apply.

9. Customer and Compliance Services, Inland Revenue (CCS) considered the original assessments were correct and that the amounts received by the Taxpayers from the sale was assessable income.

Issues | Take

10. The main issues considered in this dispute were:

- whether there was a purpose or intention of disposal at the time of acquisition of the land within the meaning of section CB 6;
- the relationship between the subdivision provisions of ss CB 6and CB 12;
- whether the amounts derived from the sale of the Units were a capital receipt due to the "identifiable capital asset principle" with the sale of the Units being analogous to the sale of a partnership interest.

11. There was also a preliminary issue as to whether the Joint Venture was also a partnership.

Decisions | Whakatau

12. The Tax Counsel Office (TCO) concluded:

- the amount derived on the sale of the Units was income under s CB 6 as the Taxpayers acquired the land with a purpose or intention of sale;
- section CB 6 can apply to the sale of the remaining land despite amounts from earlier sales of subdivided land that had been returned under s CB 12 or predecessor sections;
- section CB 6 can apply to a taxpayer selling a joint venture interest which constitutes an interest in land.

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Reasons for decisions | Pūnga o ngā whakatau

Preliminary Issue | Take tōmua tuatahi: Partnership or joint venture

13. CCS was of the view that the Joint Venture was also a partnership. The Taxpayers did not consider they were in a partnership. This issue was identified as having potential relevance to the question of whose purpose or intention is relevant in applying s CB 6.

14. While this question appeared in preliminary correspondence, neither party included this in their statements of position - as such, full arguments were not put forward. It was not necessary, on the facts, for TCO to conclude on the matter to consider the applicability of s CB 6.

Issue 1 | Take tuatahi: Purpose or intention of disposal

15. The application of s CB 6 depends upon the purpose or intention of the taxpayers at the time of purchase. This can be summarised as follows:

- In terms of the purpose or intention under s CB 6, it is the purpose or intention of a partnership rather than the individual partners.[1] A similar approach would likely apply to a joint venture.
- The land in respect of which the relevant intention must be assessed is the land in respect of which amounts were derived on disposal.[2]
- Whether the whole or part of the land originally acquired with a purpose or intention of disposal was sold, s CB 6 will still apply based on the original intention applicable on acquisition.[3]
- The provision applies even if the land is held under different legal titles or is in a different legal form.[4]
- Different purposes or intentions may be held on acquisition in respect of different parts of land, and where there is evidence as to how much of the land

[1] *CIR v Boanas* (2008) 23 NZTC 22,046 (HC).

[2] *Case L43* (1989) 11 NZTC 1,262; *Bedford Investments Ltd v CIR* [1995] NZLR 975.

[3] *Bedford Investments Ltd v CIR* [1995] NZLR 975; section CB 23B.

[4] *Case L43* (1989) 11 NZTC 1,262

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or which parts of the land were acquired with no purpose or intention of sale this land may fall outside s CB 6.[5]

- A general acknowledgement of the possibility of sale in the future is not sufficient, but a contingent or conditional purpose or intention is sufficient to trigger s CB 6.[6]
- Section CB 6 is satisfied by any purpose or intention to on-sell the land. It is not confined to a dominant purpose or intention. Accordingly, a taxpayer must show that none of their purposes or intentions were to resell or dispose of the land.[7]
- Section CB 6 may apply together with, or in the alternative, to s CB 12.[8]

16. At the date of acquisition, the Taxpayers had a purpose or intention of selling subdivided sections including the remaining land. This was to be achieved over the long term.

17. There was no other obvious purpose in respect of the remaining land as the interim activities undertaken on that land ran at a loss. No other commercial activity was pursued in relation to the remaining land.

18. While the Taxpayers did not have a purpose or intention of selling bare land, the Joint Venture had the purpose of selling or disposing of land. This was sufficient to trigger s CB 6.

19. On acquisition, no particular area of land was identified as being unsuitable for subdivision or as being held for a purpose or with an intention outside the purpose or intention of subdivision.

Issue 2 | Take tuarua: The subdivision provisions and s CB 6

20. The interaction between s CB 6 and the subdivision provisions included considering:

- whether s CB 6 was inapplicable where s CB 12 applied to treat as taxable some receipts from the earlier disposal of part of the land;

[5] *Harkness v Commissioner of Inland Revenue* (1975) 2 NZTC 61,017, *Church v Commissioner of Inland Revenue* (1992) 14 NZTC 9,1996

[6] *Case 5/2013* (2013) 26 NZTC 2-004

[7] *Case 5/2013* (2013) 26 NZTC 2-004

[8] *Case 5/2013* (2013) 26 NZTC 2-004

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- whether the application of s CB 6 is precluded by a previous classification of the land under s CB 12.

21. Section CB 12 was introduced to ensure the taxation of land where the scheme or undertaking commenced within 10 years of acquisition and did not rely upon the intention of the taxpayers at that time. If the land was acquired with a purpose or intention of selling the land, s CB 6 would apply to the land. Neither CCS nor the Taxpayers were asserting that the sale of the remaining land was taxable under s CB 12.

22. Comments recorded in Hansard[9] and the explanatory commentary on the introduction of the predecessor to s CB 12[10] do not support the view that s CB 12 prevented the application of s CB 6 if there were circumstances where both could apply. It is possible that both sections may apply.

23. TCO considered whether the cases *Simunovich*[11] and *Macfarlane*[12] cited by the Taxpayer prevented the taxation of the remaining land under s CB 6 where the amounts derived from the earlier sale of subdivided sections had been treated as taxable under s CB 12.

24. TCO concluded that these cases were not support for a broad principle that the Commissioner cannot assess differently or inconsistently from prior years. Rather, *Simunovich* supports a principle of consistency that there must be a legislative indication requiring consistent treatment. This is through a statutory link between the current characterisation and past characterisation with changes needing to be made according to the statutory method within the time bar period. There is no legislative indication in ss CB 6 and CB 12 that establishes the requisite link between the current characterisation and past characterisation of the same asset.

25. Therefore, it was concluded that s CB 6 is not precluded from applying to the remaining land just because income from the sale of some other land was earlier returned by the Taxpayers under s CB 12.

[9] Hansard (14 September 1973) 386 NZPD 3653 and 3680 – 3681.

[10] Taxation in New Zealand: report of the Taxation Review Committee" [L.N. Ross, chairman] October 1967

[11] *Simunovich Fisheries Limited v CIR* (2002) 20 NZTC 456.

[12] *Macfarlane v Commissioner of Taxes* [1923] NZLR 801

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Issue 3 | Take tuatoru: Identifiable capital asset

26. The Taxpayers argued that the sale of the Units was the sale of an identifiable capital asset and, as such, the land provisions contained in ss CB 6A to CB 23B would not apply to the sale of the underlying assets to the extent they included land. Referring to s HG 1 of the ITA 2007 and s 42 of the Tax Administration Act 1994 (TAA), they argued that a person holds a partnership interest on capital account and this is analogous to a person holding a joint venture interest.

27. Section HG 1 applies to joint ventures which are not partnerships. The section provides:

    - For tax purposes there is a flow-through of income, expenses, losses, and gains to the parties in accordance with their share. Outside of the de minimis rule in subpart HG, (the de minimis being applicable where a joint venturer's net gain on disposal is less than $50,000), the usual consequences of a sale of an asset applies.
    - The tax consequences of the disposal of a joint venture interest are the responsibility of the member.

28. Section 42 of the TAA provides that where a partnership exists, partners must make a separate return of income and deductions in accordance with their share of the partnership. Similarly, for a joint venture (which is not a partnership), s 42 provides that each member is to make a separate return considering their share of income and deductions. Regardless of whether there is a partnership or joint venture, the amount on disposal must be returned by the member in their own returns of income.

29. Neither a joint venture nor a partnership is a taxpaying entity for income tax purposes. The liability for tax on partnership or joint venture activities is that of the partner or the joint venture party. This includes in relation to any disposal an interest in land.

30. Section CB 6 can apply to a taxpayer selling a joint venture interest which includes an interest in land. TCO did not need to reach a conclusion on whether the sale of the Units was the sale of an identifiable capital asset. When each Taxpayer sold their Units, they disposed of an interest in land to which s CB 6 applied.

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