A blueprint for the interpretation of the Goods and Services Tax Act 1985 with reference to Privy Council and Supreme Court decisions

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Attestation of Authorship

I hereby declare that this submission is my own work and that, to the best of my knowledge and belief, it contains no material previously published or written by another person (except where explicitly defined in the acknowledgements), nor material which to a substantial extent has been submitted for the award of any other degree or diploma of a university or other institution of higher learning.

Yunting Lu

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Abstract

"Goods and services tax (GST) took effect on 1 October 1986. The New Zealand tax was based on the United Kingdom VAT regime, but significantly modified via fewer exemptions and a single standard rate."[1]

GST is a substantial revenue raiser for New Zealand. It has been internationally acclaimed and adopted by other countries. The framework for the tax is prescribed by the Goods and Services Tax Act 1985 ("the Act").

Under the Act, GST is charged on a supply of goods and services made in New Zealand on or after 1 October 1986 by a registered person in the course or furtherance of a taxable activity which is not an exempt supply.[2]

Given the fiscal significance of GST, the Act is a significant piece of legislation. How is this significant legislation to be read and applied? This paper interprets some of the leading court decisions.

It is, of course, the role of the courts to interpret and apply the Act. The higher the court the more authoritative the decision, and the more likely its reasoning is to be applied in subsequent cases. The decisions of the highest court – the Privy Council and, more recently, the Supreme Court – should therefore be accorded great weight when interpreting GST law. The paper therefore analyses threshold decisions of the Privy Council and the Supreme Court on the Act.

[1] A McKenzie *GST- A Practical Guide* (8th ed, CCH New Zealand Ltd, Auckland, 2008) at p vii.

[2] Section 8(1) of the Act.

There has apparently been no attempt made by commentators, courts or in other sources, to collectively analyse those decisions.

This dissertation therefore aims to fill that gap. Hence, its *first* aim is to analyse each leading Privy Council and Supreme Court decision on New Zealand GST. In the course of doing so, it extracts relevant principles which the courts utilise when interpreting and applying the Act.

The *second* aim of the paper is to formulate those resulting principles. The resulting blueprint of how New Zealand's highest court interprets and applies the Act concludes this dissertation.

The dissertation therefore ultimately provides a window to be used to interpret the Act, courtesy of the decisions of our highest court. This should provide insight for those in New Zealand who deal with GST law, and help others who are interested in GST law to intepret it. Conceivably, such a blueprint might also provide guidance to overseas countries which have adopted or are considering adopting a New Zealand style GST.

Introduction

GST is only overshadowed in importance in the New Zealand tax system by income tax. The significance of GST is two-fold.

Firstly, on the domestic front, GST comprises New Zealand's first exhaustive indirect tax. It generates some 21% of the Government tax take.[3]

Secondly, on the international scene, the New Zealand GST regime constitutes the world's 'purest' value added tax.[4] Its features of a single standard rate, very limited exemptions and zero-ratings, and simplified principles, were an international first when GST was introduced in New Zealand in 1986. The success of this format has led many other countries to study and attempt to replicate the New Zealand experience of introducing such a simple indirect tax. Leading examples include Canada, South Africa, Singapore and Australia.[5]

Given the significance of the GST regime, it is appropriate to examine *how* the courts interpret the prescribed GST rules. This dissertation attempts to do so via analysing decisions on the Act by New Zealand's highest court. Such decisions need to be considered against the backdrop of:

- the *Goods and Services Tax Act;*

- the role of the Privy Council and the Supreme Court; and

[3] The Treasury, Financial statements of the Government of New Zealand for the Year Ended 30 June 2009, Table 2, Figure 3.

[4] R Krever *GST in Retrospect & Prospect* (1st ed, Thomson Brookers, Wellington, 2007) at p1.

[5] A McKenzie, above n 1, at p ix.

- parameters, methodology and content.

The Goods and Services Tax Act

The Act prescribes the legal framework for the imposition of GST. It does this via bringing within the GST net, persons and other entities who conduct a "taxable activity" in New Zealand. The term broadly embraces a continuous or regular activity which involves making supplies for a consideration.[6]

In addition to targeting such activities, there are two notable aspects to the Act.

First, it often adopts a conceptual approach. That is, the Act frequently uses fundamental concepts to prescribe differing outcomes. Hence, as already identified, a "taxable activity" determines whether an entity might fall within the tax net. Similarly, a "supply" (or deemed supply) must usually occur to generate a 12.5% GST impost, a "going concern" might be taxed at the rate of 0%, and a "financial service" will usually be exempt (or can even be zero-rated).[7]

Secondly, the Act adopts a clearly defined and straightforward structure. Its long title reads:

> An Act to make provision for the **imposition** and **collection** of goods and services tax (emphasis added).

[6] "Taxable activity" is defined in s 6 of the Act. Generally speaking, only entities which conduct such an activity can register for the tax and are liable to account for the tax: ss 8 and 51 of the Act.

[7] Sections 3, 5, 11(1)(m), and 14 (1) (c), (1B) and (3) of the Act.

This plainly signals that the Act concentrates initially on the imposition of the tax, and then on the mechanics for collecting it from the relevant person.

This simple structure is further confirmed by the division of the Act into component Parts. Part II governs the "Imposition of Tax"; hence confirming the initial emphasis on *imposing* the tax. Part III governs "Returns and the Payment of Tax". Accordingly, Part III (and the Parts which follow it) govern the mechanics of the registered person having to account for an overall GST impost to the IRD for a regular (one, two or six monthly) period. These Parts are clearly associated with the *collection* of the tax.

In contrast, the Income Tax Act 2007 contains neither of the above features. Rather, that legislation often adopts a detailed rather than conceptual approach. (Refer, for example, to the disposition of land provisions as well as those governing qualifying companies, dividends, trusts and overseas investments.) It also adopts a more convoluted structure.

The simplicity of the GST Act arguably facilitates the formulation of a blueprint for its interpretation.

The role of the Privy Council and the Supreme Court

Before the establishment of the Supreme Court, New Zealand's highest court of appeal was the Judicial Committee of the Privy Council. Sitting in London, it dealt with a small number of appeals each year – usually fewer than ten.

The Judicial Committee of the Privy Council was traditionally the final court of appeal for many Commonwealth countries. Over time, as the various colonies

established their independence, many replaced the committee with their own court of final appeal.[8]

The Supreme Court Act 2003 came into force on 1 January 2004. It established the Supreme Court and ended appeals to the Privy Council in relation to all decisions of New Zealand courts made after 31 December 2003.[9]

It is, of course, the role of a court such as the Privy Council or Supreme Court to formulate common law and to interpret legislation. When interpreting legislation, the courts start from precisely the same premise for tax legislation as with other statutes:[10]

> The paramount question is always one of interpretation of the particular statutory provision and its application to the facts of the case.

Hence, in a tax context, the role of the court is to (i) interpret the legislation and (ii) apply that interpretation to the facts before the court. This role applies to all courts, from the highest ranked to the lowest. So why does this dissertation focus on the Privy Council and the Supreme Court judgments?

The answer is self-evident. The Privy Council and, more recently, the Supreme Court comprise New Zealand's top courts. Under the doctrine of precedent, all

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[8] Courts of New Zealand (2010) *The history of the Supreme Court*. Retrieved Sep, 3, 2009, from http://www.courtsofnz.govt.nz/about/supreme/history

[9] Refer further to ss 42 and 50 of the Supreme Court Act. See also *C of IR v Motorcorp Holdings Ltd (No 2)* (2005) 22 NZTC 19,213 (CA).

[10] *MacNiven v Westmorland Investments Ltd* [2003] 1 AC 311 at para 8 per Lord Nicholls, quoted with approval by the House of Lords in *Barclays Mercantile Business Finance Ltd v Mawson (HM Inspector of Taxes*) [2004] BTC 414 at para 8.

lower courts are bound by the core reasoning of the highest court (the ratio decidendi of the decision). Further, all other courts should accord highly persuasive status to the highest court's incidental reasoning (obiter dictum).

Accordingly, the decisions of the highest courts comprise the 'most authoritative' decisions on how to interpret and apply the Act. It is for that reason, the decisions of those courts are examined in this dissertation.

Parameters, methodology and content

The *parameters* of this dissertation are dictated by the topic – "A blueprint for the interpretation of the Goods and Services Tax Act 1985 with reference to Privy Council and Supreme Court decisions". While the paper would be more comprehensive if it reviewed GST decisions of courts at all levels, space and time limitations mean that only decisions of the highest court are examined.

The resulting *methodology* is straightforward. All GST decisions of the Privy Council and Supreme Court have been reviewed. The leading cases – those which consider the GST Act in detail – have been analysed in full. Separate chapters of this dissertation cover each of the five leading cases and the principles which they expound.

Less influential decisions, which contain limited judicial comment on the GST Act, have required a lesser analysis. They are discussed in a single chapter in this dissertation, following the discussion of the leading cases.

The principles expounded by the leading cases have then been collected together towards the end of the dissertation. They provide a basis for the concluding

blueprint for the interpretation of the Act.[11] Hence, in terms of overall methodology, the project is one of case analysis utilising a descriptive and interpretative approach.

There is no significant recourse to external material. External tax commentaries and other material have been reviewed but have been found to provide minimal assistance. This is because the overall collation of the various judgments is apparently unprecedented as are the consequential collection of principles. So the material in this paper is, by necessity, original.

Two liberties have been taken as regards the *content*. First, the cases are ordered by the nature of the courts' approach (rather than strictly chronological). Secondly, an in-depth examination has been undertaken towards the end of the paper of the Supreme Court's decision in the income tax case of *Ben Nevis.*[12] The latter is considered appropriate because (i) *Ben Nevis* is the companion case to the most significant Supreme Court GST decision, and accordingly its reasoning can arguably be imported into the GST arena and (ii) being the most authoritative Supreme Court pronouncement on interpretation of the income tax legislation, it provides a basis to test conclusions reached in this dissertation.

The balance of this dissertation is therefore ordered as follows:

- *Databank*: the founding principles;

- *Agnew*: explaining form over substance;

[11] Note that the style adopted in this dissertation is that prescribed by the New Zealand Law Style Guide rather than the APA format.

[12] *Ben Nevis Forestry Ventures Ltd v C of IR; Accent Management Ltd v C of IR* (2009) 24 NZTC 23,188.

- *Kena Kena*: the limits of form over substance;

- *Edgewater*: the limits of form over substance;

- *Glenharrow*: the extra anti-avoidance leg;

- other GST decisions of the Privy Council and Supreme Court;

- principles extracted from the cases;

- testing the principles against the approach in *Ben Nevis;*

- a "blueprint" for the interpretation of the GST Act.

Databank[13]: the founding principles

The first GST case to be decided by the Privy Council was *Databank*. The case establishes founding principles for the interpretation of the Act. It is therefore analysed thoroughly below.

Facts

The facts of the case are comparatively straightforward. Databank was a private company formed in 1967 to establish a co-operative computer service. The company was owned by the major trading banks in New Zealand.

Under an agreement with its member trading banks, Databank was to provide the trading banks with a general bank accounting and record package service consisting of a variety of electronic data processing facilities and services. The Commissioner assessed Databank for GST on its charges to the member banks for those services. Under the dispute rules then in force, Databank objected to the assessment and a case was stated to the High Court.

The High Court held that the services rendered by Databank to the banks were GST exempt financial services. The Commissioner appealed that finding to a full bench of the Court of Appeal. A three member majority of that Court held that the services supplied by Databank were financial services and were exempt from tax. The two dissenting members considered that Databank provided computer and processing services, and that those services were subject to GST.

[13] *C of I R v Databank Systems Limited* (1990) 12 NZTC 7,227.

Issue

The issue for the Privy Council was whether the services provided by Databank to the trading banks were financial services within the meaning of s 3 of the Act and so exempt by virtue of s 14(1)(a) from the tax.

Legislation

The Privy Council focused on two provisions of the Act:

- s 3 (1): the definition of financial services; and
- s 14(1)(a): financial services are exempt from GST.

Majority judgment

A four member majority decision was delivered by Lord Templeman. He found that the services provided by Databank were not financial services and were therefore subject to GST.

Legal status

Lord Templeman began his analysis by examining the agreement between Databank and the trading banks.

He noted that, under the agreement, Databank was obliged to:[14]

[14] at p 7,229.

> provide for each of the member banks a general bank accounting and record package service (known as the 'C.I.F. Package' ...) consisting of the basic services mentioned in the Schedule hereto as the same may be varied or extended from time to time by agreement.

The basic services of the CIF Package were specified in the schedule to the agreement. They comprised a full range of payment services, full customer statistical information, full customer accounting records, and full branch general ledger. Lord Templeman then proceeded to analyse other clauses in the agreement. The general tenor of the clauses was perceived as consistent with the above clauses via reinforcing the provision of a general bank accounting and record package service.

Lord Templeman then proceeded to ascertain what was actually carried out pursuant to the terms of the agreement. He referred to a brief of evidence which identified the four major activities provided by Databank to the trading banks. (The brief of evidence had been submitted by Mr Shaw who was the manager of the bank customer group of Databank.) The four activities comprised (i) providing a financial clearing system covering various types of transactions, (ii) the posting of transactions to customer accounts and maintenance of computer files of customer accounts, (iii) network management, and (iv) software support and development.

After examining the details and implementation of the agreement, Lord Templeman stated:[15]

> The provisions of the Agreement appear to provide computer services ...

[15] at p 7,229.

The writer notes that this statement already provides a clear indication as to the likely outcome of the case; namely that the contract as agreed and performed is for the provision of computer services (and not financial services) which therefore attract GST.

Lord Templeman went on to identify the first three objects of Databank's Memorandum of Association. Those objects authorised Databank to provide electronic data processing facilities, to install and operate computers and other equipment for its operations, and to record and circulate relevant statistical information.

He perceived those objects to be consistent with his analysis of the agreement. That is, the services provided by Databank to the trading banks were computer services.

Application of specific provisions

After examining the agreement (and memorandum of association), Lord Templeman turned to analyse the relevant specific provisions in the Act.

He started with s 8(1), which concerns the imposition of GST. It imposes the tax on a supply (not including an exempt supply) in New Zealand of goods and services made by a registered person in the course or furtherance of a taxable activity.

Section 6(1) defines "taxable activity". It means an activity which involves the supply of goods and services for a consideration, and includes any such activity carried on in the form of a business. Section 6(3)(d) excludes any exempt supply activity from comprising a taxable activity.

"Services" are defined under s 2 of the Act, as excluding goods and money. Section 10(2) determines the value of a supply.

Lord Templeman then applied those provisions to the facts of the case. He stated that:[16]

> Databank is a registered person, which carries on an activity in the course of a business which involves the supply of services to the banks for a money consideration pursuant to the terms of agreement … between Databank and the banks. GST is therefore payable unless Databank makes exempt services.

This brought the matter to the heart of the case. Lord Templeman observed that s 14 of the Act exempts "financial services" from GST. That term is defined in s 3 via a listing of activities which comprise financial services. The list of activities (for example) includes the exchange of currency; the issue, payment, collection, or transfer of ownership of a cheque or letter of credit; and 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 etc.

Lord Templeman examined the relevant financial services listing in detail.

He considered s 3(1)(b) of the Act. That provision includes as a financial service, "the issue, payment, collection, or transfer of ownership of a cheque or letter of credit". Databank claimed that its activities involved the "payment" and "collection" of cheques. However, Lord Templeman explained that a cheque does not order or authorise Databank to pay or collect money. Rather, a cheque orders or authorises a

[16] at p 7,230.

bank to pay or collect money. Databank, not being a financial institution, has no money which it can pay and no depository for any collection.

Hence, Databank actions are undertaken on behalf of the banks. Lord Templeman classified its actions in relation to the cheques as "a moneyless machine transmitting instructions and recording the payment and collection of cheques by banks".[17]

Lord Templeman offered a similar analysis as regards s 3(1)(ka) which embraces "the payment or collection of any amount of interest, principal, dividend …". That provision "is dealing with the payment and collection of money and not with the transmission of instructions to pay or collect money".[18] Accordingly, it did not apply to Databank.

The last provision considered was s 3(1)(ka). It covers "agreeing to do, or arranging any of the activities specified [to be 'financial services']". Databank considered that its activities were "agreeing to do, or arranging" the specified activities. For example, Databank contended that it agreed to or arranged the *payment* and *collection* of cheques.

Lord Templeman rejected this assertion. He considered that a bank may agree to pay or collect cheques. Databank does not do so. It merely records the effect of any agreements or arrangements made by the banks for the specified activities. He stated:[19]

[17] at p 7,231.

[18] ibid.

[19] Ibid.

> There are two separate contracts, the contract between a bank and its customers, whereunder the bank supplies financial services, and the contract by a bank with Databank whereunder Databank provides computer services.

Lord Templeman then expanded on this point by providing a great example to illustrate the relationship between Databank and the banks. Before computers were invented, the clerical work of carrying out the instructions of customers and banks with regard to cheques drawn by customers on the bank was performed by clerks and couriers. Now, all the clerical works are performed by computers, which mechanically and automatically obey instructions from banks which are programmed into the computer system. A cheque is not *paid* until a bank reduces its indebtedness to customers' accounts and a cheque is not *collected* until a bank increases its indebtedness to a customer.

All that Databank does, then, is supply the bank with the services of a computer which replaces the services of the banks' employees.

Lord Templeman concluded his review of the specific provisions by stating that there is nothing in the agreement, and no evidence was produced, to indicate that Databank carries on any of the activities under s 3(1) of the Act or possesses the resources or the authority or the desire to do so.

Rejection of the reasoning of the High Court and of the majority of the Court of Appeal

The Privy Council noted that Davison CJ in the High Court[20], and the majority of the Court of Appeal (Cooke P, Somers and Casey JJ)[21], had held in separate judgments that Databank provided financial services. Lord Templeman rejected the reasoning of each.

The High Court had proceeded on the basis that Databank was "involved" in the provision of financial services and therefore had provided such services. Lord Templeman considered that the word "involved" was not to be found in the Act. The test was whether Databank provided the express service stipulated in the Act. It did not.

In the Court of Appeal, Cooke P adopted a similar approach to Davison CJ in the High Court. He also asserted that "the services performed by Databank as agents for the trading banks are part of the financial services provided by those banks to their customers, and accordingly are exempt from the tax".[22] The Privy Council considered that Cooke P had misconstrued the agency provisions. Section 60 of the Act merely provided that a supply made by an agent to a third party on behalf of a principal was deemed to be made by the principal. Section 60 did not apply here because Databank never made a supply to a third party (but only to the trading banks).

Both Somers and Casey JJ had also adopted an approach similar to the High Court. Somers J held that Databank and the banks "collectively provided" financial services. Casey J considered that Databank's functions were an "integral part" of the financial service activities.

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[20] *Databank Systems Ltd v C of IR* (1987) 9 NZTC 6,213.

[21] *C of IR v Databank Systems Ltd* (1989) 11 NZTC 6,093.

[22] at p 6,101.

The Privy Council rejected both analyses. This was on the basis that Databank provided an independent standalone service (and not a collective supply with the banks to the banks' customers). So there were two contracts here; one of computer services by Databank to the banks and the other being the provision of financial services by the banks to their customers. The legislation was not concerned with collective supplies, nor did it provide that just because a bank conducted an exempt activity, a person who made supplies to that bank would also be deemed to be making exempt supplies.

Endorsement of the minority judgments of the Court of Appeal

While rejecting the views of the High Court and the majority of the Court of Appeal, Lord Templeman expressly endorsed the view of the minority of the Court of Appeal. He stated:[23]

> Their Lordships agree with the minority judgments and with the analysis of Richardson J who stated at p 6,105 that in his opinion Databank:
>
> '…provides its customer trading banks with computing and other services which enable those banks to provide financial services to their customers.'

The 1989 amending Act

[23] at p 7,235.

Lord Templeman concluded his judgment by referring to the 1989 amending Act. That amending Act legislatively reversed the effect of the Court of Appeal decision (but not retrospectively). Databank argued that the amendment was only necessary if the original form of the legislation effectively provided that Databank services were GST exempt financial services. That is, the fact that an amendment Act had to be passed in order to render Databank's services taxable, evidenced that Databank's services were not taxable prior to the amending Act.

This argument was resisted by the majority of the Privy Council. Their view was that clarifying legislation does not alter the interpretation of the legislation which existed before the clarifying legislation was passed. Hence an 'avoidance of doubt' provision does not alter the reading of other provisions of the Act.

Comment on and significance of *Databank*

The majority of the Privy Council judgment in *Databank* was unequivocal in its reasoning and findings. However, at no stage did Lord Templeman actually prescribe that he was adopting a certain approach to interpreting and applying the legislation. He did not offer an overall rationale to his approach, such as saying "The approach entails looking at this issue and then approaching it in this manner". Neither did he flag where he was going via using headings.

He simply proceeded with his judgment. Nevertheless, it is contended that important principles can be extracted from the judgment. The writer considers that her comments on such principles can be grouped under three headings:

- Legal status
- Application of specific statutory provisions

- Other interpretation principles.

The significance of the case is then discussed.

Legal status

The judgment of the majority of the Privy Council commenced with an examination of the contract between Databank and the banks. It examined the contract in terms of what had been *entered into and carried out*. (Refer to pp 16-17 of this dissertation, "Legal status".)

The legal effect of that contract then represented the facts as ascertained.

It is considered that Lord Templeman's approach simply reflects a standard approach to ascertaining facts for taxation cases. In particular, it is contended that his approach is entirely consistent with the leading New Zealand statement on interpreting the facts in a taxation context. That is the statement of the law by Richardson J in *Marac Life*:[24]

> The true nature of a transaction can only be ascertained by careful consideration of the legal arrangements actually *entered into and carried out*: not on an assessment of the broad substance of the transaction measured by the results intended and achieved or of the overall economic consequences. The nomenclature used by the parties is not decisive and what is crucial is the ascertainment of the legal rights and duties which are actually created by the transaction into which the parties entered. The surrounding circumstances may be taken into account in characterising the transaction. Not to deny or contradict the written agreement but in order to understand the setting in which it

[24] *Marac Life Assurance Ltd v C of IR; C of IR v Marac Life Assurance Ltd* (1986) 8 NZTC 5,086 at p 5,097.

was made and to construe it against that factual background having regard to the genesis and objectively the aim of the transaction. (emphasis added)

Hence, the writer considers that *Databank* establishes that the facts of a case are ascertained with reference to the legal arrangements entered into and carried out by the parties.

Application of specific statutory provisions

After ascertaining the facts with reference to the legal arrangements entered into and carried out, Lord Templeman proceeded to apply specific statutory provisions to those facts. This is evidenced by his examination of ss 6 and 8 etc, which would have the effect of rendering Databank's supplies taxable. He then followed with an examination more especially of the listings of various "financial services" in s 3(1), which could have exempted the Databank services.

That approach is detailed earlier in this dissertation (pp 18-21, "Application of specific provisions"). It is also largely confirmed by Lord Templeman's statement that:[25]

> *There is nothing in the Agreement* dated 17th July 1969 and no evidence was produced *to indicate that Databank carries on any of the activities specified in sec 3(1) of the Act* or possesses the resources or the authority or the desire to do so. By the Agreement, Databank is a supplier of computer services to banks and not a supplier of financial services to banks or customers. (italics added)

[25] at p 7,232.

It is considered that examining the facts and applying the statutory provisions is simply a standard approach to interpreting tax legislation (and indeed other forms of legislation). This contention finds support from a more recent pronouncement by the House of Lords that:[26]

> The paramount question is always one of interpretation of the particular statutory provision and its application to the facts of the case.

Accordingly, the *Databank* approach calls for an assessment of the facts (with reference to the legal arrangements entered into) in conjunction with an application of the relevant statutory provisions to those facts.

Other interpretation principles

As stated, the majority of the Privy Council applied the relevant statutory principles to the facts. However, Lord Templeman's judgment recognised that other factors apart from the plain wording of the specific provisions can play a part in statutory interpretation.

Intention

Lord Templeman commented on the intention of the Act. He did so in the following passage:[27]

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[26] *MacNiven v Westmorland Investments Ltd* and *Barclays Mercantile Business Finance Ltd v Mawson (HM Inspector of Taxes*) as per n 9 above.

[27] at p 7,234.

> By sec 20 of the Act of 1985 a supplier must account to the Revenue at the end of every taxable period for the difference between input tax suffered by him and output tax charged by him during the period. By sec 2 input tax in relation to a registered person means tax charged under sec 8(1) of the Act on the supply of goods and services to that person. Correspondingly output tax in relation to a registered person means tax charged pursuant to sec 8(1) of the Act in respect of the supply of goods and services made by that person. The Act does not provide that in calculating the difference between input and output tax a supplier shall be entitled to deduct input tax suffered by him in respect of a non-exempt supply made to him in the course of or for the purpose of enabling him to supply exempt services.
>
> The provisions relating to input and output tax are inconsistent with any intention of Parliament to grant an exemption not only for financial services supplied by the bank but also in respect of taxable services supplied to the bank.
>
> In 1989 Parliament passed an amending Act which negatived for the future the construction of the Act which had found favour with the majority of the Court of Appeal. Although the 1989 Act cannot be employed to construe the Act of 1985, it appears from the 1989 Act that in 1989, at any rate, Parliament was unwilling to allow a wider exemption than that for which the minority contended.

Hence, Lord Templeman considered the intention of Parliament twice; first in relation to how the provisions of the statute interacted and, secondly, in relation to an amending Act. He considered that the intention of the Parliament supported a conclusion that GST applied to the supply made by Databank.

Intention, scheme and language

The first two paragraphs of the above quote necessitates further comment. What Lord Templeman is saying here is that input tax and output tax rules apply with

reference to supplies made by the taxpayer (and that the effect of those rules is not dependent on who the taxpayer makes supplies to). He is thus using the 'scheme' of the input tax and output tax provisions to influence the reading of the financial services provisions.

Accordingly, Lord Templeman recognises that both intention and scheme can play a part in interpreting the Act.

This contention is also reinforced by another aspect of his judgment. As noted previously, Lord Templeman expressly approves the minority judgments in the Court of Appeal. While a detailed examination of the minority judgments is outside the scope of this dissertation, those judgments heavily emphasise that intention and scheme are also leading statutory interpretation influences. Both dissenting judgments even go as far as to nominate what the scheme of the Act is.

Their combined effect in this regard can be summarised as:

a) The principles of interpreting a tax statute are no different from the principles for interpreting any other statute. (Refer to the judgment of McMullin J and the passage which he quotes from *Attorney-General v Carlton Bank* [1899] 2 QB 158.)

b) When interpreting a tax (or other) statute, effect is to be given to the intention of Parliament. That intent is to be gauged from the language used, and also the relevant context or 'scheme' of the legislation. (Refer more especially to the judgment of McMullin J and the passage which he quotes from *Attorney-General v Carlton Bank*.)

c) The scheme of the GST Act is to tax the supply of goods and services by a registered person in the course of a taxable activity which that person carries on (McMullin J). Or, to put it another way, the tax is focused on the supply by a supplier to a recipient so that it is a "transaction based" tax (Richardson J).

d) English and other overseas VAT and GST case law has limited application to New Zealand GST. This is because the language and scheme of the New Zealand legislation differs from overseas versions. (Both Richardson and McMullin JJ.)

The endorsement of these two judgments by Lord Templeman presumably extends to these principles expounded by Richardson and McMullin JJ.

Accordingly, both the approach adopted by Lord Templeman and his endorsement of the minority Court of Appeal judgments, evidence that interpretation of the Act is effected via words of the Act, the purpose of the Act and the scheme of the Act.

Of course, such a construction is entirely consistent with statutory direction on how to interpret legislation (s 5(j) of the Acts Interpretation Act 1924 and s 5 of the Interpretation Act 1999). Similarly, with the leading New Zealand judicial statement on statutory interpretation: "the true meaning [of the specific provision] must be consonant with the words used, having regard to their context in the Act as a whole, and to the purpose of the legislation to the extent that this is discernible."[28]

Scheme

[28] *C of IR v Alcan New Zealand Ltd* (1994) 16 NTZTC 11,175 at p 11,179 per McKay J for the Court of Appeal.

Also of significance is that the minority Court of Appeal judgments identified and used the scheme of the GST Act to determine the issue. Both members undertook an analysis of that scheme, and (as mentioned in paragraph (c) above) concluded that it was a 'supply' or 'transaction based' tax. When doing so, they concentrated on the interaction of the charging provisions and the exemption provisions in Part II of the Act.

Given that the scheme of the Act focused on supplies or transactions, the Act was to be applied with reference to the nature of the supply made by the supplier to the recipient. Or, in other words, the supply made by Databank to the banks should be examined in isolation (and not integrated with the supply made by the banks to their customers).

Under this approach, the service provided by Databank to the trading banks was a computer service, but the services provided by trading banks to their customers were financial services.

Hence, the scheme of the Act was important; it necessitated that each transaction be examined separately and with reference to the nature of supply.

This approach has also been validated by other case law. For example, in *Chatham Islands Enterprise Trust*[29], Keith and Blanchard JJ stated that: "The tax being one on transactions, it is necessary to pay close attention to the legal nature of what has been done." In the same case, Tipping J stated: "GST is payable on transactions. When deciding whether a particular transaction is of a kind which attracts GST, it is important to analyse carefully its legal characteristics."[30]

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[29] *Chatham Islands Enterprise Trust v C of IR* (1999) 19 NZTC 15,075 at [17].

[30] at [25].

The scheme approach therefore not only recognises that the GST Act is transaction based, but also requires that the relevant transaction be analysed with reference to the legal nature of the transaction.

The Privy Council judgment, via endorsing the minority Court of Appeal judgments, indicates it acceptance of this scheme analysis.

As an aside, the writer contends that the scheme of the Act identified by the minority of the Court of Appeal – viz a supply or transaction tax – applies more readily when the relevant provision of the Act is primarily concerned with the status of a "supply". Hence, in *Databank*, the issue was whether supplies made by Databank had the quality of "financial services". The quality of the "supply" will often be the focus under Part II of the Act, which deals with the "Imposition of Tax". However, it is less likely to the situation under Part III of the Act ("Return and Payment of Tax") and subsequent Parts. Accordingly, the scheme approach might be less applicable in this latter situation. For GST "imposition" cases, however, the scheme seems to be more influential than the purpose and language of the Act.

Classification of the Privy Council approach

The writer considers, then, that the Privy Council approach to interpreting the Act has incorporated the three components referred to above.

Obviously, the *language* of the statute was emphasised when Lord Templeman considered the application of s 3(1). (See the discussion above under the heading "Application of specific provisions".)

The *intention* of the legislation was specifically referred to by Lord Templeman in the quote reproduced above (under the heading "Intention"). That it was a factor in the Court's reasoning is further confirmed by another quote: "Their Lordships have been unable to find anything in the Act which indicates that Parliament intended to exempt anything other than the supply of financial services or that Parliament intended that all or any of the costs incurred by the banks in supplying financial services should be exempt from GST." [31]

The *scheme* of the input tax and output tax provisions was used to ascertain the intention of Parliament ("Scheme" above). Further, Lord Templeman specifically endorsed the minority judgments, which adopted a schematic approach.

Thus, the approach used by Lord Templeman incorporated wording, intention and scheme. The writer terms this approach, the 'traditional purposive approach' (it will be contrasted with the 'more purposive approach' in a later chapter).

Correctness of the approach

The writer agrees with the approach adopted by Lord Templeman.

Its correctness is illustrated with reference to the rejection of the reasoning of the High Court and the majority of the Court of Appeal. They had contended that the Databank services comprised an "integral part" of the banks' financial activities or that the banks and Databank made "collective" supplies of financial services to the banks' customers. If the broad substance or economic consequence is considered, the Databank service might be an integral part of the ultimate services provided by

[31] at p 7,234.

the banks to their customers (or there might be a collective supply). However, that is not the correct way to examine the facts of the case.

The actual issue was the quality of the supply made by Databank (ie, was it a supply of financial services?). This called for an assessment of the contracts made at law and performed in reality ('entered into and carried out'). There were plainly two contracts of a different nature. The Databank contract with the banks was plainly one for the provision of computer services. The banks one with its customers was plainly one of financial services.

The legislation focused on the quality of the supply via using such words as "supply" (in ss 6, 8(1) and 14). It did *not* provide for "collective supplies" nor did it say that where a supply made by one person comprised an integral part of a supply made by a second person, the two supplies should be considered jointly. Neither did the intent or scheme of the legislation so provide. Accordingly, the decision of the majority was correct, as was the approach they took.

Significance

The analysis of *Databank* so far has contended that:

- The facts of a GST case are determined by the 'legal status' of the underlying transaction.

- The courts then apply the specific statutory provisions to those facts.

- When applying the specific statutory provisions, regard is had not only to the words of the provisions, but also to the purpose and scheme of the Act.

- The scheme of the Act focuses on a supply made by a supplier to a recipient; the tax is transaction based.

On the basis of that analysis, it is considered that *Databank* is a highly significant case. Not only did it determine the financial service issue regarding Databank, but it also defined the appropriate approach to interpreting and applying the GST Act.

Whether these founding principles are consistent with subsequent Privy Council and Supreme Court decisions is considered in the balance of this paper.

Minority judgment

Lord Ackner delivered a sole dissenting judgment in the Privy Council. In essence, he adopted an approach similar to that of the High Court and the majority of the Court of Appeal. For instance, he stated that there "was ample evidence demonstrating that Databank's functions are an integral part of the various activities going to make up the definition of 'financial services' in sec 3(1), and as such can be regarded as an extension of the trading bank's normal functions, constituting an important part thereof."[32]

A fuller analysis of the dissenting judgment is unnecessary. This is because the majority of the Privy Council decision comprises an authoritative approach to interpreting the GST Act, and Lord Ackner's dissenting approach has never been subsequently applied.

[32] at p 7,239.

Principles extracted from *Databank*

The writer has placed into three categories principles extracted from Databank.

Firstly, are key principles, which comprise principles central to the courts' approach to interpreting and applying the Act. Secondly, are further and supplementary principles concerning factual analysis. Thirdly, are further and subsidiary principles of interpretation of the Act.

These principles summarise the central ideas from *Databank* on interpretation.

Key Principles

The key principles are:

- When ascertaining the relevant facts, it is appropriate to examine the legal arrangements entered into and carried out (this was the approach of the majority of the Privy Council).

- When interpreting the GST Act, the courts primarily examine purpose, scheme and language (the approach of the majority of the Privy Council, and also the approach of McMullin J in the Court of Appeal as endorsed by the majority of the Privy Council).

- The scheme of the GST Act is transaction based (Richardson and McMullin JJ in the Court of Appeal as endorsed by the majority of Privy Council) and therefore each transaction has to be analysed separately. For example, there is a supply made by Databank to the banks, and another supply made by trading banks to customers, because there are two separate transactions.

A further principle concerning facts

There is a single supplementary principle regarding factual analysis:

- A form over substance approach is to be applied when ascertaining facts (the majority judgment applies this approach).

Further principles of interpretation

Further statutory interpretation points are:

- The GST Act and other fiscal legislation are interpreted in the same manner as other statutes (McMullin J, as endorsed by the majority of the Privy Council).

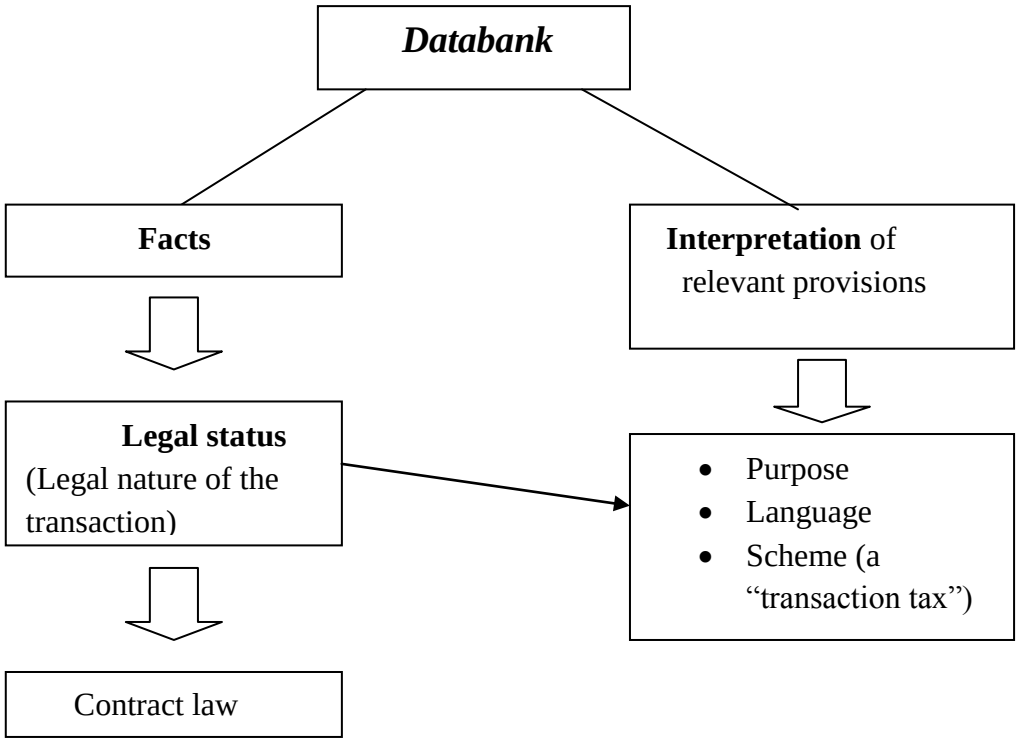
- The scheme of the GST Act apparently applies readily when the statutory direction is concerned with the quality of the supply (such as is usually the case with Part II of the Act, "Imposition of Tax"). It might not apply so readily to other Parts of the Act.

- For GST 'imposition' cases, the analysis of scheme seems to be more influential than the analysis of the purpose and language of the Act.

- Overseas VAT and GST cases have limited application to New Zealand GST given the differing language and scheme of the legislation.

Diagram

The key principles are extracted from Databank are incorporated into the below diagram.



Agnew[33]: explaining form over substance

In *Databank*, the approach used by Lord Templeman can be clearly ascertained, in order to decide whether the service provided by Databank is one of financial or computer services. His first step was to analyse the contract between the parties, in order to ascertain the legal obligations which the parties had entered into and carried out. Having ascertained the legal status of the contract, he then applied the relevant statutory provisions (in accordance with the purpose, scheme and language of the Act).

Obviously, then, the legal status of the contract is crucial given that it comprises the first step in interpreting and applying the Act. However, Lord Templeman did not specifically identify *how* a contract is to be interpreted. The case of *Agnew* elaborates on how a contract should be interpreted. The case, at its heart, explains the contractual interpretation approach used in *Databank*, and illustrates how this approach works.

The case concerned the priority of interests under s 42 of the Act. More specifically, whether GST claimed by the Commissioner in respect of a company in receivership would prevail over the interests of a party holding a charge over the company. Whichever interest had priority, would then determine whether available funds would be paid to the Commissioner or the charge holder.

Under the language of s 42 as it then applied, the issue reduced down to whether the charge was a "fixed or a floating charge". This phrase was to be interpreted with reference to the common law status of the charge. The writer notes that s 42 has subsequently been amended and that the *Agnew* decision no longer has relevance to

[33] *Agnew v C of IR* (2001) 20 NZTC 17,192.

the present version. However, the case is instructive in prescribing how a document (in this case the charge over the contract) is to be interpreted.

Facts

The brief facts of the case are that the taxpayers were receivers of a company and had been appointed by a bank pursuant to a debenture issued by the company. Under the terms of the debenture, a fixed charge was created over book debts and a floating charge was created over their proceeds.

The only assets available for distribution to creditors were the proceeds of the book debts which were outstanding when the receivers were appointed and which they had since collected. If the charge was a fixed charge, as the receivers contended, the proceeds were payable to the company's bank as the holder of the charge. If it was a floating charge at the time it created, then the proceeds were payable to the Commissioner (and also the employees of the company) as preferential creditors.

Issue

The issue was whether a charge over the uncollected book debts of a company, which leaves the company free to collect them and use the proceeds in the ordinary course of its business, was a fixed charge or floating charge.

Legislation

The court focused on the following provisions:

- the Companies Act 1993: The Seventh Schedule;
- the Receiverships Act 1993: s30; and

- the GST Act 1985: s 42 (Recovery of tax).

Judgment

The unanimous decision of the Privy Council was delivered by Lord Millet. It largely focused on how to interpret a document.

The Court examined an earlier decision by the English Court of Appeal on *how* to determine whether a floating or fixed charge existed (*In Re New Bullas*[34]). That case held that the stated intentions of the party, as recorded in the document, determined whether there was a fixed or floating charge. Lord Millet described the Court of Appeal reasoning in *New Bullas* as follows:[35]

> It was clear from the descriptions which the parties attached to the charges that they had intended to create a fixed charge over the book debts while they were uncollected and a floating charge over the proceeds. It was open to the parties to do so, and freedom of contract prevailed.

The proposition adopted in *New Bullas* accordingly was that the parties could determine the legal status of a document simply by specifying that they intended a certain outcome, and by ensuring that the language of the document was consistent with that intended outcome.

Lord Millet strongly rejected this approach. He advocated an alternative two-stage analysis:[36]

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[34] *In Re New Bullas Trading Ltd* [1994] BCC 36; [1994] 1 BCLC 449.

[35] at [31] of his judgment.

[36] at [32].

> At the first stage, the court must construe the instrument or charge and seek to gather the intentions of the parties from the language they have used. But the object at this stage is not to discover whether the parties intended to create a fixed or a floating charge. It is to ascertain the nature of the rights and obligations which the parties intended to grant each other in respect of the charged assets. Once these have been ascertained, the court can embark on the second stage of the process which is one of categorisation. This is a matter of law.

By saying this, the court means that the first thing is to look at the legal rights and obligations the parties intended to create. Then, secondly, the court classifies the document as a matter of law based on those legal rights and obligations.

The Privy Council then used the 'licence versus lease' common law to further illustrate this two stage process. Lord Millet stated:[37]

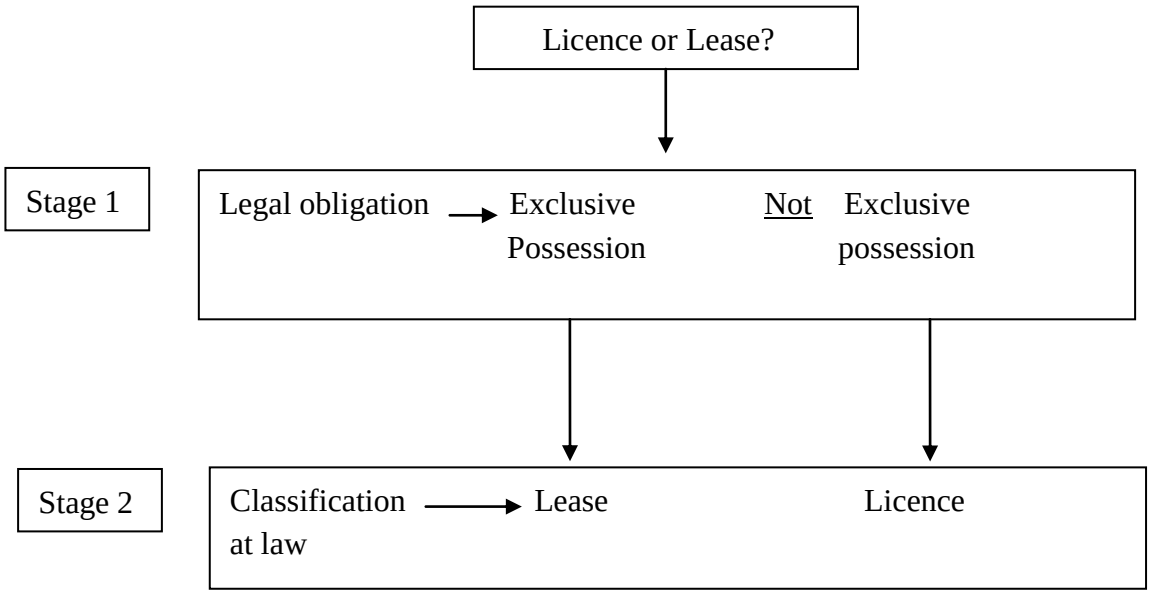
> A similar process is involved in construing a document to see whether it creates a licence or tenancy. The court must construe the grant to ascertain the intention of the parties: but the only intention which is relevant is the intention to grant exclusive possession.

Hence, the issue in respect of whether a document creates a licence or lease is *not* a single stage enquiry of 'did the parties intend to create a lease (or licence) and did they use language throughout that document which showed that they intended to create a lease (or licence)'.

[37] Ibid.

Rather it is a two stage enquiry. Stage one concerns the legal rights and obligations which the parties intended to create – in this case, did they intend to grant exclusive possession? Stage two is then to classify that legal right and obligation as a matter of law – in this case, the intended effect of granting exclusive possession is that a lease (as opposed to a licence) has been created as a matter of law. It matters not that the parties have headed the document up "licence", have used the phrase "licence" throughout the document and have even stated that they specifically intend to create a licence and not a lease.

The below diagram reinforces both (i) this illustration and (ii) the *Agnew* "two stage" analysis of documents:



The Privy Council in *Agnew* therefore determined the facts of the case via the legal rights and obligations in force and their resulting classification at law. Application of this two stage approach by the Court resulted in the document before it being classified as a floating charge.

Comment on and significance of *Agnew*

The approach of the Privy Council in *Databank* was to ascertain the facts of the case with reference to the legal rights and obligations entered into and carried out.
It concluded that the rights and obligations entered into and carried out generated a supply of computer services. (It then applied the provisions of the GST Act to that supply.)

The Privy Council's approach in *Agnew* elaborates on how to classify a document under common law. Its two stage analysis builds a further step into how courts ascertain facts for the purposes of applying the New Zealand GST Act. That further step simply means that facts are now to be ascertained by reference to (i) the rights and obligations created and (ii) as classified as a matter of law. It is illustrated in a further diagram below ("Principles extracted from Agnew").

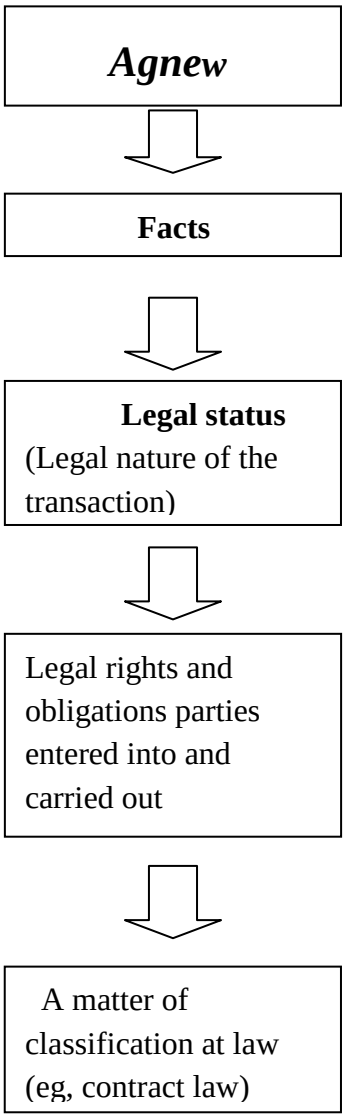
Principles extracted from *Agnew*

Two key principles are taken from *Agnew*. They are:

- A two stage process is used for interpreting documents: the first stage is to determine what are legal rights and obligations that the parties have entered into and carried out, and the second is to classify those rights and obligations at law.

- This approach could be applied to many GST cases, such as *Databank*.

These key principles are illustrated via the following diagram:


Agnew
Facts
Legal status
(Legal nature of the transaction)
Legal rights and obligations parties entered into and carried out
A matter of classification at law (eg, contract law)

Kena Kena[38]*:* the limits of form over substance

The approach adopted in *Databank* and *Agnew* advocates (in part) ascertaining the facts of the case with reference to the legal form adopted by the parties. The writer calls this the 'classic approach'. However, there are some exceptions to this classic approach. *Kena Kena* explains one of those exceptions.

Facts

The facts of the case are uncomplicated. The taxpayer company, KKP, operated a rest home. KKP joined the rest home subsidy scheme when the Minister of Social Welfare established it in 1989. The purpose of the scheme was to subsidise the cost of providing rest home accommodation for needy elderly people. A rest home proprietor who joined the scheme agreed to provide eligible residents with a certain level of accommodation and services. In return the proprietor would be paid a fee (including a subsidy by the Department of Social Welfare) which did not exceed the 'maximum fee-for-service rate' fixed by the Department.

When the fee-for-service rate was first determined in 1989, the calculation took into account the fact that GST (then 10%) would be payable by the rest home proprietor at a discounted rate of 8.2% on the fees they charged. Almost immediately after the agreement was signed, the general rate of GST was increased to 12.5% (discounted to 10.25% for rest homes).[39]

[38] *Kena Kena Properties Ltd v Attorney-General* (2002) 20 NZTC 17,433.

[39] Section 10(6) of the Act provides that a discounted rate applies to rest home and other "commercial accommodation" providers.

The contract between KKP and the Department came to an end in 1993. In January 1999, KKP commenced proceedings. It claimed that the Department should have increased the sums paid to KKP to reflect the increase in GST.

Issue and arguments

The issue was whether the Department should have adjusted the sums paid to KKP to reflect the increase in GST. This in turn depended on whether monies paid by the Department to KKP were "in the nature of a grant or subsidy", and thus outside the second proviso to s 78(2) of the Act. That proviso states that where a public authority contracts for the supply of goods and services where the consideration is in the form of a grant or subsidy, the public authority is not required to change the consideration to match a change in the rate of GST.

KKP argued that the payment by the Department was in fact a normal consideration for the supply of services rendered by it and so was not in the nature of a grant or subsidy. The Department argued that the payment was plainly that of a subsidy.

Legislation

The court was only concerned with a single provision, being the second proviso to s 78(2) of the Act.

Majority judgment

The Privy Council was split 3-2 on the issue. Lord Hoffmann delivered the majority judgment (the other members of the majority being Lord Nicholls and Lord Millet).

Contractual analysis

Lord Hoffmann referred to several clauses in the agreement made between KKP and the Department, which related to the "rest home subsidy scheme". However, leaving aside the fact that the document was entered into under the scheme, there was nothing in the document which was of prime relevance.

Interpretation of the legislation

Lord Hoffmann then moved on to the interpretation of the relevant provision.

He noted that the disagreement was about the words "in the nature of a grant or subsidy" in the second proviso to s 78(2) of the Act. The proviso specifies that the increase of GST rate will not apply in respect of any supply of goods and services where the consideration for that supply is in the nature of a grant or subsidy.

In the Department's view, its payments to KKP were under a subsidy scheme and were therefore "in the nature of a grant or subsidy".

However, KKP argued that it was simply paid a commercial rate for the services which it provided under the contract. While there was a subsidy, it was a subsidy by the Department to the *residents* and not to the rest home proprietor. The words "in the nature of a grant or subsidy" only referred to a subsidy received by the *supplier* of the services. As it was the resident which ultimately received the benefit of the subsidy (via not having to make a payment to the rest home proprietor), the rest home did not receive such a subsidy but rather was simply paid a normal fee for its services.

Lord Hoffmann stated that most grants or subsidies will be paid to public charitable or private bodies in order to confer benefits upon third parties. They are paid

because it is considered in the public interest to enable such bodies to provide accommodation, health services, cultural events and so forth to members of the public at concessionary rates. A subsidy received by a person for the benefit of a third party, was still a subsidy paid to the person receiving it. Accordingly, it was the rest home proprietor who the Department paid the subsidy to.

KKP also argued that the proviso would only apply where the party providing the service in return for the grant or subsidy, although not itself the beneficiary, was a non-profit making organisation. KKP, on the other hand, was a commercial company; it provided the service for the Department in the same way as it would have provided a similar service to a privately-funded resident.

Lord Hoffmann rejected this argument because it relied upon a distinction between "commercial" and "non-profit making" recipients which was very hard to find in the statutory language. By saying this, he meant that what is set out in the provision is what the legislation actually meant.

Accordingly, Lord Hoffmann simply applied the plain wording of the Act in holding that the payment of a subsidy by a Government agency was "in the nature of a grant or subsidy".

Comment on and significance of *Kena Kena*

The approach adopted by Lord Hoffmann is plainly different from that used in *Databank.*

The 'traditional purposive approach' adopted in *Databank* involved the analysis of the legal status of the transaction first, followed by the interpretation of the

legislation (in accordance with the purpose, language and scheme of the Act). However, Lord Hoffmann did not undertake an in-depth analysis of the relevant contract (but simply referred to several clauses in passing). Instead, he focused on the relevant legislative provision and applied it to the facts of the case. Hence, he held the legislative direction was to ascertain whether a "subsidy" was paid, and that this legislative direction was met as a question of fact. There was no need to undertake a contractual analysis given this clear statutory direction.

The writer considers that Lord Hoffmann's approach in this case is appropriate. This is because the main issue did not relate to the contractual interpretation of the facts, but simply called for an interpretation of the legislation and its application to the plain facts.

In contrast, *Databank* was concerned with the imposition and collection of GST and whether or not the relevant "supply" attracted GST. As was pointed out by Richardson J in that case, the scheme of ss 3, 6, 8 and 14 is that of a "supply" or "transaction" tax. Thus each transaction/supply had to be examined individually. Similarly, in *Agnew*, the legislation gave a direction to consider whether the document was a fixed or floating charge, and this also necessitated an examination of the legal status of the document.

Kena Kena therefore provides an example of an exception to the traditional purposive approach of *Databank*; where the facts of the case are not ascertained by a legal analysis of the underlying document. As mentioned, the exception arises where the particular provision of the Act directs the factual enquiry away from the status of the underlying transaction/contract. In that case, the factual enquiry was one of whether the payer had paid a "subsidy".

Minority judgment

Let us now take a look at why the dissenting judges reached a different decision, what the reason is behind their decision, and whether it is due to a fundamentally different approach.

The dissenting judgment was jointly delivered by Lord Hobhouse and Lord Scott.

The judgment is divided into two parts, one being the contractual interpretation, and the other being the interpretation of the legislation.

Under the contractual interpretation part, the judgment identifies that there are two contractual parties; the Department and the rest home licensee (Contractor). The document is headed "rest home subsidy scheme".

The judges then examine the function of each contractual party. The Contractor is a commercial profit-making concern and has standard fees which it charges for its services. The Department is responsible for administering a publicly funded scheme for providing financial support to those in need of such rest home facilities and who cannot themselves afford to pay for those services. The Department will make up the difference between what the resident can afford to pay and the amount of the rest home fees. The judgment went on to examine some relevant clauses in the agreement between the Contractor and the Department.

Their Lordships then argued that "the statutory obligation to pay the 'subsidy' is an obligation imposed by statute upon the Department in favour of the qualifying recipient – providing financial support for eligible rest home residents".[40]

[40] at [20].

They then held that:[41]

> The Department is making a payment to the contractor in consideration of the supply of the service; there is no element of subsidy involved. No more than the market value of the service is being paid … The only nature which the sums paid to the Contractor has is that of reasonable commercial consideration for the supply of a service.

By stating this, they simply mean that the money paid by the Department was for the service rendered, thus it will be considered as having the same nature as what the rest home gets for services provided to other people who can afford to pay themselves, and therefore no element of grant or subsidy is involved.

When it comes to the interpretation of the legislation, the judgment argues that since the Contractor asks for the payment of the agreed consideration for the supply, the Contractor does not seek any subsidy or grant from the Department. It is simply a normal commercial fee.

The judgment also asserts that the primary purpose of s 78(2) is the achievement of a fair adjustment of the price as between supplier and purchaser to take account of the increased cost to the supplier of making the supply. In keeping with this purpose, the Contractor should be compensated for the increased GST impost.

Comment

This decision of the majority stands as correct law and the decision of the minority has not been endorsed (as far as this writer is aware) in any subsequent case. The

[41] ibid.

writer considers that the minority approach is, with respect, contrary to the plain legislative direction provided by the second proviso to s 78(2).

As can be seen from the judgment, the minority has used the *Databank* 'traditional purposive approach', by examining the contracts entered into between the parties, and then applying the relevant specific legislation (by reference to the purpose and language of the Act).

In particular, the minority state that the money paid by the Department is for the service supplied by the rest home to the resident. This is similar to *Databank*, where Lord Templeman endorsed the supply analysis by Richardson J in the Court of Appeal, held that there were two separate supplies and that the nature of the two supplies were different (see further, pp 20-23 of this dissertation). Lord Templeman then referred back to the contract to examine the nature of the supply made by Databank to determine whether it was a computer or financial service. In the present case, the minority judgment similarly followed the supply analysis to determine that the money was for the supply of a rest home service. That is, the minority examined the transaction principally from a "supply" perspective.

In the writer's opinion, this approach is not applicable in this case, since the main issue is related to the language of the specific provision ("in the nature of grant or subsidy"). The legislative focus is on whether the funds paid by the Department are in the nature of grant or subsidy. (Refer more especially to the following language in the second proviso: "shall not apply to require a public authority to alter any amount [paid] where the consideration for the supply is in the nature of a grant or subsidy".) The focus then is on the quality of the payment from the perspective of the Government agency. It is not necessary here to undertake a contractual interpretation.

In fact, the legislation will give a direction when a contractual interpretation should be adopted. Such as in the case of *Databank*, the main provisions included ss 8 and 14, and both sections are concerned with the word "supply". This signals that the case is concerned about the nature of the "supply" and that it will be necessary to undertake a contractual interpretation.

However, in the present case of *Kena Kena*, the dispute concerns the wording of the legislation only. The relevant provision is not about supply, and it is not necessary to interpret the contract by reference to the supply concept. Thus, it can be said, when it is the situation of GST imposition, the contractual interpretation must be taken into account. However, for situations which only relate to the uncertain wording of the legislation, there might be no need to adopt a contractual analysis (or analyse the legal nature of the transaction).

Edgewater[42]*:* The limits of form over substance

Edgewater concerns the liability of a mortgagee to account for GST on a mortgagee sale.

At first glance, it appears to be a highly significant GST case. However, when scrutinised, it simply involves the straightforward application of specific provisions of the GST Act. This is evidenced by the fact that the Privy Council delivered a unanimous and brief judgment confirming the unanimous (and brief) judgment of the New Zealand Court of Appeal.[43]

Edgewater confirms the approach of the majority of the Privy Council in *Kena Kena*; that, on occasions, the GST Act does not require an examination of the legal status of a transaction.

Facts

The facts of the case are straightforward. A first mortgagee effected a mortgagee sale where the vendor/mortgagor was GST registered. Section 5(2) of the Act deems a mortgagee sale to be a supply and s 17(1) renders the mortgagee liable to file a return and account to the Commissioner for any GST imposed on the sale.

However, the proceeds of the mortgagee sale were insufficient to cover both the total mortgage debt on the property and the GST impost on the sale.

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[42] *Edgewater Motel Ltd v C of IR* (2004) 21 NZTC 18,664.

[43] *C of IR v Edgewater Motel Ltd* (2002) 20 NZTC 17,984 (CA).

The case was to determine whether all the proceeds of the sale could be retained by the mortgagees or whether the first mortgagee was personally liable to pay the GST impost out of the sale proceeds.

Issue

The primary issue was whether a mortgagee who sells land under the power of sale is liable for any GST imposed on the sale.

Legislation

The Privy Council examined the following provisions of the GST Act:

- s 5(2): meaning of term supply – sale in satisfaction of debt;
- s 17: special returns – (the mortgagee must pay the GST); and
- s 42: recovery of debt.

It also referred to s 104 of the Land Transfer Act 1952 which sets out the order of priorities under a mortgagee sale.

Judgment

Lord Hoffmann delivered the judgment. He referred to the facts briefly. He then set out the effect of s 5(2) (imposing a prima facie GST impost on a forced sale) and s 17(1) (making the mortgagee or other person effecting the sale liable to file a special return and pay the Commissioner the GST impost on the forced sale).

Lord Hoffman then stated, on the first page of his brief judgment:[44]

> The language [of ss 5(2) and 17(1)] could hardly be clearer. Although a sale by a mortgagee is deemed to be a supply in the course of a taxable activity carried on by the mortgagor, it is the mortgagee who must pay the tax.

He then proceeded to dispose of an argument which had found favour in the High Court.[45] Baragwanath J, in the High Court, had examined the effect of s 104 of the Land Transfer Act. That provision sets out the priorities for the application of the proceeds of a mortgagee sale. The first priority under s 104 is "the expenses occasioned by the sale".

The High Court held that GST was not an "expense occasioned by the sale", but it was a tax levied on the supplier. As such, the priority ordering under s 104 required that the sale proceeds be applied to the discharge of mortgages before any GST was paid to the Commissioner. This meant that if there were insufficient funds to cover both the mortgages and the GST impost, the funds could be applied exclusively to discharge the mortgages.

However, Lord Hoffmann rejected this contention. He stated that s 17 of the GST Act "simply says that [the mortgagee] must pay the GST".[46] The debt, being a personal one of the mortgagee arising as a result of the sale, was therefore an "expense occasioned by the sale":[47]

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[44] at [6].

[45] *Edgewater Motel Ltd v C of IR* (2002) 20 NZTC 17,713 (HC).

[46] at [10].

[47] at [12].

> Their Lordships consider that [the GST impost] is plainly an 'expense occasioned by the sale' within the meaning of [s 104 of the Land Transfer Act].

Accordingly, it was in keeping with the effect of s 104, that the mortgagee pays the GST liability out of the mortgagee sale proceeds.

There was a further supplementary point to the case. It was held that where the sale proceeds were sufficient to cover a first mortgage and the GST impost, but not the second mortgage, the first mortgagee could apply the funds to the payment of the GST, and was not accountable to the second mortgagee for the amount of the GST payment. That is, the second mortgagee could not sue the first mortgagee simply because the first mortgagee paid GST to the Commissioner.

Comment on and significance of *Edgewater*

In this case, Lord Hoffmann – as he did for the majority of the Privy Council in *Kena Kena* – only dealt with the interpretation of the relevant specific provisions of the Act, and did not analyse the legal status of the underlying transaction or document. This is for the same reason as in *Kena Kena*. That is, there is a specific statutory direction which does not require a factual assessment to be made of the nature of the underlying transaction or documentation.

In *Edgewater*, the sole factual issue (which was not in dispute) was that there was a mortgagee who had effected a mortgagee sale which was subject to GST. The Privy Council held that the interpretation of the relevant legislation in the light of those facts was straightforward.

Edgewater is significant because it determines that a mortgagee is personally liable for the GST on a mortgagee sale. It also reinforces that the GST Act sometimes does not require a detailed analysis of the underlying contract or documentation.

Principles extracted from *Kena Kena* and *Edgewater*

Both *Kena Kena* and *Edgewater* establish that there are limits to the 'traditional purposive approach' of *Databank*. This is because both cases are concerned with the interpretation of legislation only and do not necessitate that the 'facts' be established with reference to the legal arrangements entered into and carried out. In my view, this is more likely to arise when Part II of the Act ("Imposition of Tax") is not being considered given that the emphasis in Part II is on 'supplies' and therefore requires an examination of the underlying transaction/document.

Kena Kena and *Edgewater* therefore generate the following two key principles:

- The approach used in *Databank* sometimes does not apply. On occasions, the Act does not require an examination of the legal nature of the transaction. This arises where there is a specific statutory direction which does not require a factual assessment to be made of the nature of the underlying transaction or documentation.

- This 'exception' apparently more readily applies if a case is not concerned with an imposition issue.

Glenharrow[48]: The extra anti-avoidance leg

As mentioned, the 'traditional purposive approach' adopted in *Databank* might not apply to every GST case. *Kena Kena* and *Edgewater* provide exceptions. In contrast, *Glenharrow* apparently reinforces the *Databank* approach, while adding an extra step to it in the case of tax avoidance.

Glenharrow is the leading GST avoidance case. It also represents the first (and to date only) detailed decision of the Supreme Court on the GST Act.

Facts

The facts concern the sale and purchase of a mining licence and the resulting secondhand goods input tax credit claimed by the purchaser.

The licence had been purchased by a Mr Meates for $10,000. He subsequently sold it for $45m to a company not associated with him, called Glenharrow Holdings Ltd ("Glenharrow"). At the time of sale the mining licence had only three years left to run. Settlement of the sale was effected largely by way of cheque swap and mortgage back.

As Mr Meates was not registered for GST, the purchasing company claimed a secondhand goods input tax credit based on the $45m purchase price.

These facts are elaborated on more fully below as part of the process of identifying the approach adopted by the Supreme Court (under the heading "Legal status").

[48] *Glenharrow Holdings Ltd v C of IR* (2009) 24 NZTC 23,236.

Issues

The issues in the case were:

(i) Whether the input tax credit claimed by Glenharrow was deductible.

(ii) Whether the input tax claim comprised tax avoidance.

Legislation

The Court focused on the following provisions of the Act:

- s 2: the definition of "input tax";
- s 10: value of supply of goods and services;
- s 20(2): valuation of tax payable – no deduction without required documentation;
- s 24 (2): invoice created by recipient;
- s 75: the definition of keeping of records; and
- s76: tax avoidance.

Judgment

The unanimous judgment of the Supreme Court was delivered by Blanchard J. It comprised a reasonably full analysis (some 55 paragraphs).

Legal status

The Court commenced its judgment by referring to the facts of the case (which have already been summarised above). It focused on three legal documents – the licence

per se, its sale and the mortgage back documentation – and on the surrounding circumstances.

The Court noted that the mining licence was issued on 15 November 1990 for a term of 10 years. The licence permitted the mining of serpentinite, bowenite and certain other rock.

The licence changed hands in 1993 and again in 1994 before Mr Meates purchased it in December 1996 for $10,000. At no stage was Mr Meates registered for GST (or liable to be registered).

Early in 1997, Mr Meates was approached by Mr Gerard Fahey about selling the licence to his company, Glenharrow. Mr Fahey knew something of the history of the old quarry and had formed the view that there was at least half a million tonnes of serpentinite and bowenite within the licence area. They agreed on a sale price of $45m. Mr Fahey considered the actual value of the licence to be higher, and was supported in this by an informal valuation done by his cousin who had studied valuation as part of an MBA degree.

The documenting of the sale between Mr Meates and Glenharrow was done in a very informal way. On 28 June 1997, apparently without first seeking professional advice, Mr Meates wrote and Mr Fahey countersigned a letter to a Christchurch solicitor, Mr Pengelly, recording the agreement of Mr Meates to sell the licence to Glenharrow. The price was $45m. It comprised a deposit of $80,000 and a mortgage back to Mr Meates for the balance of the price. The mortgage was to be over the licence, and also the company's assets and the shares in the company. There was to be interest at 10% per annum but not during the first two years because "it will take

two years for the mining operation to get organised". There was to be no repayment of capital for three years.

After the parties received legal advice, the terms were changed somewhat. A mortgage of the licence was executed on 22 August 1997 and, seemingly overlooking the payment of the deposit, provided for three annual payments of $15m beginning on 31 March 1999 without interest (but with penalty interest for late payment). Later on 14 November 1997, a deed of sale was completed in which the deposit payment was acknowledged and settlement for the balance of the monies was effected by the exchange of cheques with a mortgage back over the licence and other (negligible) company assets.

The other document which the Court mentioned was a deed of mortgage of the shares of Glenharrow. Mr Fahey executed it on 31 November 1997 as a security for the $44,920,000. A reading of it gives the impression that Mr Fahey was making himself personally liable for that sum. He covenants that Glenharrow will repay it, and there is no express exclusion of personal liability. It was, however, the evidence of both Mr Fahey and Mr Meates that no such liability on the part of Mr Fahey was intended.

Accordingly, the liability to pay the $44,920,000 was solely that of Glenharrow. That company had a share capital of $100. Its debt to Mr Meates was to be paid from the proceeds of the mining.

Glenharrow claimed a secondhand goods input tax credit on the $45m purchase price. It subsequently transpired that (contrary to the understanding of the parties) the licence was not able at law to be renewed. Before the licence expired, Glenharrow was only able to extract a limited quantity of stone and make further

payments to Mr Meates totalling $210,000. It defaulted on the balance owing and no further monies were recovered by Mr Meates.

Application of specific provisions – allowing an input tax credit

After the analysis of the relevant transactions, the Court considered "the position of the parties under the GST Act before the question of avoidance is reached".[49] It examined the relevant provisions of the Act.

It stated that the GST Act taxes supplies of goods and services by registered persons in the course of their taxable activities. "Taxable activity" is defined under s 6 of the Act and embraces a "continuous or regular activity".

Section 2 of the Act defines the term "goods" as "all kinds of personal or real property other than choses in action or money". The Court considered that the mining licence was "secondhand goods" (as that term is defined in s 2).

Section 51 of the Act stipulates that every person who carries on a taxable activity is liable to be registered. Mr Meates did not carry on any such "continuous or regular" taxable activity. Hence, he did not have to be GST registered (and was not). Glenharrow, however, was correctly registered for GST because its actual mining activities comprised a "continuous or regular" activity.

Section 24 provides that it is the person who makes the supply who must provide the recipient with a tax invoice. However, s 24(7) applies where a supplier makes a supply, not being a taxable supply, of secondhand goods to a recipient who is a registered person. Here, the recipient must maintain sufficient supporting records

[49] at [15].

(as set out in s 75). If it has done so, then according to s 20(2)(c), the recipient will be entitled to claim an input tax deduction in respect of the supply of the licence of an amount equal to the tax fraction of the consideration in money for that supply. That is provided the licence was acquired by the recipient "for the principal purpose of making taxable supplies". Glenharrow had that principal purpose and had retained the requisite records.

Section 10 provides for the "value of supply". Where the parties are not associated, the value of supply is the "amount of money". The price paid was plainly $45m and was therefore the value of the supply of the licence.

Glenharrow was therefore entitled to a secondhand goods credit based on the purchase price of $45 m (leaving aside the issue of tax avoidance).

Hence, the Supreme Court applied the relevant specific provisions to the legal form of the transactions.

Section 76 – purpose of the Act

The input tax credit therefore stands under the normal provisions of the Act. Justice Blanchard then considered the application of s 76, the general anti-avoidance rule (GAAR).

The Court was dealing with the form of s 76 which applied before 2000. (The provision was amended in 2000 to bring it more into line with the income tax avoidance provisions.) Blanchard J focused on the following wording of that

provision: "[an arrangement] entered into between persons to defeat the intent and application [of the GST Act or any provision of the Act]".[50]

He noted that:[51]

> There is a two-stage process before the Commissioner can carry out a reconstruction under s 76. First, the Commissioner must have been justified in coming to the view that there was an 'arrangement' … Secondly, the Commissioner must have been properly satisfied that the arrangement was entered into between the parties to it to defeat the intent and application of the Act or any provision of the Act.

As regards the first stage of the process, the Court stated that whether there had been an "arrangement" was never in issue. In its view, there was certainly an arrangement between Mr Meates, Glenharrow and Mr Fahey. The Court then spent a considerable time setting out its views on the second stage, viz whether that arrangement "was entered into to defeat the intent and application of the Act or any or any provision of the Act".

This called for, in the Court's opinion, an assessment of the purpose of the *arrangement* as opposed to the purpose of the *parties*. That is, it required an objective and not a subjective assessment of purpose. That process involved "considering the effect which the arrangement has had – what it has achieved – and then, by working backwards as it were from the effect, you are able to determine what objectively the arrangement must be taken to have had as its purpose."[52]

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[50] at [34].

[51] at [35].

[52] at [38].

Hence, the purpose of the arrangement can be deduced entirely from the underlying document.

Once that purpose is ascertained, it is applied to see if it breaches the intent and application of the legislation. In this regard, Blanchard J stated:[53]

> The intention of the Act will be defeated if an arrangement has been structured to enable the avoidance of output tax, or the obtaining of an input deduction in circumstances where that consequence is outside the *purpose and contemplation of the relevant statutory provisions*. Lord Hoffmann in *C of IR v Auckland Harbour Board* (2001) 20 NZTC 17,008 (PC) at [11] commented that, generally speaking, GAARs were:
>
> > 'aimed at transactions which in commercial terms fall within the charge to tax but have been, intentionally or otherwise, structured in such a way that on a purely juristic analysis they do not. This is what is meant by defeating the intention and application of the statute.'
>
> An arrangement of this kind is not in accordance with the overall purpose of the Act because it produces a 'tax advantage' *not within the contemplation of the statute*. (italics added)

This then necessitated a discussion of whether the input credit claimed by Glenharrow was "within the contemplation of the statute".

Was the present transaction "within the contemplation of the Act"?

[53] at [40].

The Court commenced this discussion by noting that, at a policy level, the GST tax was intended to be broad-based, efficient and neutral.

The tax also meant that registered persons producing taxable supplies effectively operate as tax collectors on behalf of the Government and as such are not themselves subject to GST's economic incidence. The Court noted that:[54]

> That is of course consistent with the neutrality and efficiency of the revenue collection rationales that underlie the Act. The corollary is that registered persons should, by the same token, not obtain *unacceptable windfall gains* from the regime. (emphasis added)

The Court then explained the operation of the secondhand goods input tax credit. It identified two types of transactions as producing "unacceptable windfall gains".

Firstly, where the parties inflate the price so that the purchaser secures an (enhanced) input tax credit. Secondly, where the transaction is structured to obtain an artificially early deduction.

It considered:[55]

> [These] transactions have *artificial feature*s combined with *advantageous tax consequences* not contemplated by the scheme and purpose of the Act. (italics added)

It then held that the transaction entered into by Glenharrow had this effect.

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[54] at [43].

[55] at [48].

That transaction had "artificial features". This is because while the price was 'paid' at law, it was not paid in economic terms. Rather, in economic terms, there was no consideration in money given by Glenharrow because of the commercial impossibility of payment by it in circumstances where it was virtually uncapitalised, its debt obligation was not supported by its shareholder, and the three year period left to run on the licence meant that only a fraction of the mortgage debt would ever be paid. Hence, it was not the price here which created the distorting feature but the method of 'payment'.

The transaction also had "an advantageous tax consequence" not contemplated by the scheme and purpose of the Act. This was because the transaction produced "a GST refund totally disproportionate to the economic burden undertaken by Glenharrow or the economic benefit obtained by Mr Meates."[56]

Accordingly, the transaction was to be struck down as comprising tax avoidance. The input tax claim would be based only on the amount paid in cash by Glenharrow. (That is, the deposit of $80,000, plus the further sum of $210,000 paid to reduce the debt.)

Comment on and significance of *Glenharrow*

As mentioned previously, *Glenharrow* comprises the Supreme Court's first – and to date only – extensive consideration of an issue under the GST Act.

It is possible to divide the approach into two separate steps.

[56] at [54].

The *Databank* approach

Before considering the tax avoidance issue, the Supreme Court applied the same approach as in *Databank*. That is, the Supreme Court examined the legal effect of the transaction and applied the Act to that legal form.

This is evidenced by the Court exploring the legal rights and obligations which arose under the contract entered into by Mr Meates and Glenharrow. For example, that:

- The contract provided for the sale and purchase of a mining licence, which had only three more years to run before it expired.

- That "payment" had been effected in terms of legal form via cheque swap and mortgage back.

'Extra leg'

Unlike the case of *Databank*, however, the present case involved an 'extra leg'.

In *Databank*, Lord Templeman analysed the legal nature of the transaction, with reference to the legal rights and obligations which the parties entered into and carried out. He did not need to consider tax avoidance because the relevant arrangement was not aimed at defeating the intention of Parliament.

As mentioned above, a similar analysis was undertaken in *Glenharrow*. However, its facts were suggestive of tax avoidance. Because what Glenharrow actually paid in cash was different from what it claimed, an artificial element was involved which enhanced the amount of the tax deduction. This then led the Court (for tax

avoidance purposes) to analyse the facts in accordance with true economic sacrifice. More precisely, while payment for the purchase had been effected in legal terms, it had not been effected in economic terms (and this resulted in the transaction being struck down from a tax avoidance perspective). Not only was tax avoidance therefore added as an extra leg, but a different measuring stick was then applied (economic sacrifice as opposed to legal form).

Hence it can be said that, if a case is not suggestive of tax avoidance such as *Databank*, the examination of the legal nature of the transaction will be the only thing to take into consideration when ascertaining the 'facts'. However, if the facts are suggestive of tax avoidance, a second leg comes into play. This additional step necessitates an analysis of the purpose of the arrangement (measured objectively), to see if the purpose of the arrangement is defeat the intent and application of the Act. Commercial and economic yardsticks can apply here.

An extra step has therefore being added to the 'traditional purposive approach' where the case is suggestive of tax avoidance.

Principles extracted from *Glenharrow*

Glenharrow established both key principles and additional interpretation principles.

Key principles

As can be seen from the above discussion, *Glenharrow* establishes two key principles:

- Before the consideration of tax avoidance, the approach works in the same way as in *Databank* ie, the legal nature of the transaction is ascertained, then

the relevant provisions of the Act are interpreted and applied to the legal form of the transaction. The Act is interpreted in accordance with its purpose, scheme, and language.

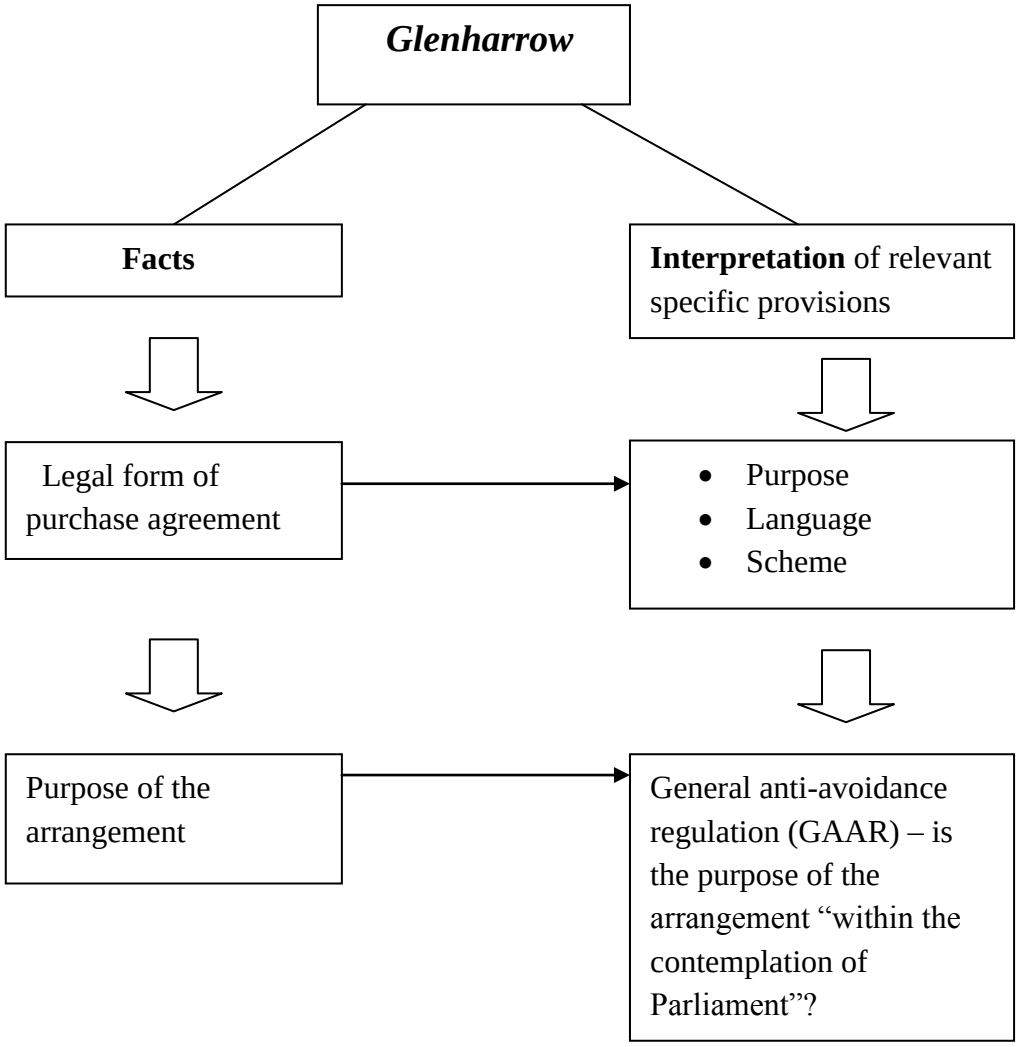
- In circumstances where a tax avoidance issue is involved, an ‘extra leg’ is added to the approach. This calls for an objective assessment of the purpose of the arrangement, and then ascertaining whether the economic consequence (or broad substance) of that arrangement produces an outcome not contemplated by Parliament.

Further principles of interpretation of the Act

Further interpretation principles apply in relation to the application of GAARs. Perhaps the most prominent for GST avoidance cases, is that the analysis of the purpose of the Act - or what was ‘within Parliament’s contemplation’ - is more important than the analysis of the scheme and language of the Act. If the objective intention of the arrangement is to defeat the purpose of the Act, then the GAARs will normally be invoked.

Diagram

The below diagram illustrates the key principles arising from *Glenharrow*.


Glenharrow
Facts
Interpretation of relevant specific provisions
Legal form of purchase agreement
Purpose
Language
Scheme
Purpose of the arrangement
General anti-avoidance regulation (GAAR) – is the purpose of the arrangement "within the contemplation of Parliament"?

Other GST cases

For the sake of completeness, it is necessary to acknowledge that there are other decisions of the Supreme Court on GST. However, it is considered that they have limited application to the present topic.

The writer has divided the cases into three categories.

First, procedural cases, usually being those concerning an application by a taxpayer for leave to appeal to the Supreme Court (ie, are not a full hearing). Such cases have been reviewed by the writer and have been found to contain no significant comment on interpreting the GST Act. Examples include *Lopas*[57] and *Ch'elle Properties*.[58]

The second group is the criminal cases. They do not fall under the present topic because they are decided under the Tax Administration Act 1994 (ie, are not decided under the GST Act); the present approach concerns only the interpretation of the GST Act. The criminal cases include *Gilchrist*[59] and *Smith*.[60]

The third group is the contract law cases. Once again, these cases are not concerned with the provisions of the GST Act, and thus do not fall within the ambit of an assignment concerning the interpretation of the GST Act. Examples of this category include the two *Southbourne* cases.[61]

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[57] *Lopas v C of IR* (2006) 22 NZTC 20,010.

[58] *Ch'elle Properties (NZ) Ltd v C of IR* (2007) 23 NZTC 21,653.

[59] *Gilchrist v R* (2007) 23 NZTC 21,150.

[60] *Smith v R* (2009) 24 NZTC 23,176.

[61] *Southbourne Investments Ltd v Greenmount Manufacturing Ltd* (2007) 23 NZTC 21,270; *Southbourne Investments Ltd v Greenmount Manufacturing Ltd* (No2) (2007) 23 NZTC 21,514.

Accordingly, all such cases provide limited assistance because none of them comprises a full decision of the Court on the interpretation of the GST Act.

GST cases – the basic structure of interpretation

This dissertation has so far reviewed in depth five leading GST cases. Those cases provide a defined structure for the interpretation and application of the GST Act.

Facts of the case are to be determined by reference to the legal status of the relevant transaction. This approach was applied in *Databank*. It was subsequently confirmed in *Agnew* and *Glenharrow*.

Interpretation of the statute is then undertaken. This is done with regard to the wording of the specific statutory provisions, coupled with the purpose and scheme of the Act. Again, *Databank* establishes this approach and *Glenharrow* reinforces it.

The combination of the above two steps comprises the 'traditional purposive approach'. That approach is, however, modified where statutory directions dictate that the facts are to be ascertained with reference to matters other than the legal status of the supply. *Kena Kena* and *Edgewater* illustrate this exception.

Further, an extra step can apply to the traditional purposive approach. *Glenharrow* identifies that the extra step arises when the facts are suggestive of tax avoidance.

This then is the basic structure generated by the five leading cases. Obviously, other principles build on and supplement the basic structure. Those other principles have been detailed at the conclusion of the discussion of each case and will be collected together and set out later in this paper ("Principles extracted from above cases"). For the moment, however, the validity of the basic structure is tested via a full review of the recent income tax case, *Ben Nevis*.

Ben Nevis[62]: Testing the principles

Introduction

Ben Nevis is a leading case in the area of tax avoidance and New Zealand income tax. Despite its income tax origins, it can be viewed as a companion case to *Glenharrow*. This is because *Ben Nevis* and *Glenharrow* were both decided by the same Court, the two judgments were delivered on the same day, they both concern tax avoidance issues, and four out of five justices were the same.

Moreover, there has traditionally been a substantial overlap between the courts' approach to the income tax legislation and the GST Act. A straightforward example is the application of the approach adopted by Richardson J in *Marac Life*[63] where he set out his classic statement on how to interpret facts with reference to legal arrangements entered into and carried out; this has been quoted and applied extensively by the Court of Appeal and other courts in both an income tax and a GST context. Refer, for example, to the Court of Appeal decisions in the income tax cases of *Buckley & Young*[64] and *McKenzies*[65] and that Court's GST decisions of *Gulf Harbour*, *New Zealand Refining*[66] and *Turakina Maori Girls College*.[67]

The fact that *Ben Nevis* and *Glenharrow* are companion cases, and the fact that the courts often take a common approach to income tax and GST legislation, means that *Ben Nevis* can be used as a 'benchmark' to test the basic structure advanced by the GST cases. Undertaking this exercise, first calls for an examination of that case.

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62 *Ben Nevis Forestry Ventures Ltd v C of IR; Accent Management Ltd v C of IR*, above n 11.

63 *Marac Life Assurance Ltd v C of IR; C of IR v Marac Life Assurance Ltd*, above n 23.

64 *Buckley & Young Ltd v C of IR* (1978) 3 NZTC 61,271.

65 *C of IR v McKenzies New Zealand Ltd* (1988) 10 NZTC 5,233.

66 *New Zealand Refining Co Ltd v C of IR* (1982) 5 NZTC 61,176.

67 *Turakina Maori Girls College Board of Trustees v C of IR* (1993) 15 NZTC 10,032.

Facts, issues and legislation

The facts, issue and legislation in this case are not particularly relevant to the present paper. This is because the case is not directly concerned with the GST Act. The most notable features here for present purposes are:

(i) The facts involved a highly convoluted structure which generated ongoing income tax deductions without an equivalent cash input for the investor. (The relevant documentation will be referred to when examining the judgments; not so much to set out the facts but more to illustrate the approach adopted by the Court.)

(ii) There were two issues: were the claimed deductions allowable under the relevant provisions of the Income Tax Act 1994 and (if so) were they struck down under the relevant anti-avoidance provisions?

Note that all section references for the Income Tax Act are to the 1994 version (being the applicable legislation for *Ben Nevis*).

Majority judgment

There are two set of judgments, one representing Tipping, McGrath and Gault JJ, the other delivered by Elias CJ and Anderson J. While the ultimate outcome of the case is the same, their approach to the first issue – that of whether the deduction is allowed under the relevant provisions of the Income Tax Act – differs.

The judgment representing Tipping, McGrath and Gault JJ used the ‘traditional purposive approach’. (It will referred to as the ‘majority judgment’.) The latter two justices used what the majority referred to as the ‘more purposive approach’. (It will be referred to as the ‘minority judgment’.)

The two approaches are detailed below.

Legal status

While the majority judgment represented the views of Tipping, McGrath and Gault JJ, it was delivered by the first two mentioned judges. Their approach, in the writer’s view, conformed with the traditional purposive approach used by Lord Templeman in *Databank*.

The majority started with the facts of the case. They did so more especially by examining the legal rights and obligations that the parties entered into and carried out.

This included a detailed examination of the terms and conditions of agreements entered into by the investors who claimed the income tax deductions. Relevant documentation examined included a grant of licence and separate licence agreements entered into by the investors with the owner of forestry land, and an insurance agreement between the investors (via an intermediary) and a company called CSI Insurance Group (BVI) Ltd (“CSI”). The agreements were entered into in 1997 and they generally ran for a 50 year period (up until 2048). Their combined effect was to provide detailed rules governing an investment (including the management, growing and sale of trees) and covering relevant financial aspects (including sale proceeds, expenses and insurance). The investment produced

favourable income tax deductions for the investors when compared with their cash input.

As mentioned, the majority scrutinised the details of the relevant contracts in order to ascertain the resulting legal rights and obligations. Hence, for example, they closely examined the terms of the insurance contract. This included (inter alia) identifying that the insurance would be triggered in the event that the market value of stumpage of Douglas Fir did not reach $2,050,518 per plantable hectare during the period between occurrence of the event and 31 December 2048. The syndicate (of investors) was obliged to pay two premiums on the insurance to CSI. The first premium was to be paid in 1997, and the second by 31 December 2047. If the net stumpage did not reach the expected value, compensation would be paid by the insurance company.

After examining the terms of the agreement, the majority concluded that an insurance agreement existed, which insured the investors for up to $2,050,518 per plantable hectare in the event that the net stumpage did not reach this value. While this might seem a logical conclusion, the method of arriving at it is instructive.

According to the majority judgment:[68]

> When considering the application of a specific tax provision, before reaching any question of avoidance, the Court is concerned primarily with the legal structures and obligations the parties have created and not with conducting an analysis in terms of their economic substance and consequences.

[68] at [47].

This means that in order to decide whether the deduction is allowed, the first thing is to look at the legal rights and obligations which the parties entered into. In this case, as can be seen from the agreement, it was an insurance service provided by CSI to the taxpayers.

This reflects the approach of *Databank*, where Lord Templeman went straight into analysing the agreement between Databank and the trading banks, and ascertained that the service provided by Databank is a computer service which is different from the service provided by the trading banks. And this approach is also reflected by that used in *Agnew*. There, Lord Hoffmann carried out a two stage process in order to examine the legal status (stage one being the analysis of the legal rights and obligations that the parties had entered into and carried out: stage two being the resulting classification of the contract at law with reference to those rights and obligations). In keeping with the emphasis of the Privy Council in *Databank* and *Agnew* on legal form, the majority of the Supreme Court in *Ben Nevis* rejected an analysis based on the broad substance or economic consequence of the transaction.

The form over substance approach is further confirmed by another passage of the majority's judgment:[69]

> The Court must construe the relevant documents, in their commercial context, to ascertain the parties' obligations to each other, as if it were determining a dispute between them over the meaning and effect of their contractual arrangement.

Obviously, the quote upholds the form over substance approach via stipulating that where a document generates a certain legal effect, that legal effect will be the same across various areas of law. For example, a 'lease' will be a lease and not a 'licence'

[69] at [46].

for land law purposes, for contract law purposes, and for taxation purposes. Hence, the legal status of a particular transaction will be the same across all areas of law (in the absence of statutory intervention).

Application of the specific provisions

> Once the nature of the contractual rights and obligations has been determined in this way, the specific provision can be applied.[70]

This statement by the majority is, in the writer's view, the same approach as used in *Databank*. In that case, Lord Templeman, after determining that computer services were provided by Databank to the trading banks by reference to the agreement entered into, applied the specific provisions of the Act to impose GST on the computer services.

One example of its application in the present case concerned the grant of the licence. The majority judgment analysed the document via referring to its clauses, and ascertained that it provided for a payment of a licence premium. Having established that the payment was for the right to access land under a licence, the majority then concluded that the payment was for a "right to use land" under the relevant provisions of the Income Tax Act (ss EG 1, OB 1 definition of "depreciable property", and Schedule 17). Therefore the premium was deductible as depreciation on depreciable property under those specific provisions before the question of tax avoidance was taken into the consideration.[71]

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[70] at [48].

[71] at [54].

The remaining issue was therefore the application of the anti-avoidance provisions to the relevant deductions. (The deductions included those for the insurance premium and licence premium.)

Anti-avoidance provisions – purpose of the Act

The majority commenced its tax avoidance analysis by setting out the relevant provisions: s BG 1 which it stated "must be read with the definitions in s OB 1 of 'arrangement', 'tax avoidance' and 'tax avoidance arrangement'."[72]

It then undertook a detailed examination of the history of the income tax anti-avoidance provisions, and also of the 'scheme and purpose' approach which the courts had applied to those provisions.

A detailed description of that statute and case law is beyond the ambit of this paper. However, it is of some relevance to note that the majority endorsed the following statement by Richardson J in *Challenge Corporation*:[73]

> [Interpreting the relevant provisions] is a matter of statutory construction and the twin pillars on which the approach to statutes mandated by s 5(j) of the Acts Interpretation Act 1924 rests are the scheme of the legislation and the relevant objectives of the legislation.

The majority found that other case law was consistent with this scheme and purpose approach,[74] such as the Privy Council judgments in *Peterson v C of IR*.[75] It also

[72] at [69].

[73] *Challenge Corporation v C of IR* [1986] 2 NZLR 513.

[74] at [98].

[75] *Peterson v C of IR* [2006] 3 NZLR 433

noted that s 5 of the Interpretation Act 1999 supports "the need for a wider perspective".[76]

Following its review of such case law, the majority prescribed its approach (broadly reflective of the scheme and purpose approach):[77]

> [I]f it is apparent that the taxpayer has used the specific provision, and thereby altered the incidence of income tax, in a way which cannot have been *within the contemplation and purpose of Parliament* when it enacted the provision, the arrangement will be a tax avoidance arrangement. (italics added)

Accordingly, the focus becomes were the relevant transactions within the purpose and contemplation of Parliament?

Were the present transactions within the contemplation of Parliament?

The majority then set out their approach to ascertaining whether the effect of the arrangements were within the contemplation and purpose of Parliament:[78]

> [Here,] the Commissioner and the courts may address a number of relevant factors, the significance of which will depend on the particular facts. The manner in which the arrangement is carried out will often be an important consideration. So will the role of all relevant parties and any relationship they may have with the taxpayer. *The economic and commercial effect of documents and transactions may also be significant…* A classic indicator of a use that is outside Parliamentary contemplation is the structuring of an arrangement so that the taxpayer gains the benefit of the specific

[76] at [99].

[77] at [107].

[78] at [108].

> provision in an artificial or contrived way. It is not within Parliament's purpose for specific provisions to be used in that manner. (italics added)

The application of this approach is briefly discussed below with reference to the grant of licence.

In the present case, for their 1998 income year, the investors claimed a deduction for "depreciable property" in respect of the licence premium. The amount deducted was approximately $41,000 for each plantable hectare in which they had invested. However, their actual cash expenditure for that year was only $50 per plantable hectare (paid as a licence fee). The investors contended that the expenditure on the licence premium was incurred when promissory notes were executed (during 1997).

The majority were prepared to proceed on the basis that an expense of $41,000 for each plantable hectare was "incurred" in the 1998 income year. They then stated that "[t]he *commercial aspects* must, however, be considered because the context is suggestive of tax avoidance" (italics added).[79] Under a commercial analysis, there was an artificial element in the arrangement because the promissory notes were executed and 'given' before the expenditure was incurred in reality. Hence, from a business point of view, the promissory notes were a gratuitous mechanism.

The majority also highlighted two other features of the arrangement.[80] The first was that there was a real risk the Trinity scheme would never be profitable. The second was the timing mismatch between when the expenditure is legally incurred and the point when it is required to be paid in the economic sense.

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[79] at [119].

[80] at [120].

The majority concluded their analysis of the avoidance status of the licence premium as follows:[81]

> The result of this use of the specific provision is to take the arrangement, insofar as it depends on the licence premium promissory note, outside of the scope of the provision allowing for a deduction for depreciable property and to make what the investors entered into a tax avoidance arrangement.

A similar logic and outcome was applied to other components of the investment.

Embracing the two step approach

It can be seen from the above discussion that the majority clearly adopted and endorsed a two step approach. That is, to firstly consider the legal status of the documents and to apply the specific provisions of the legislation and, secondly, to consider the application of GAARs where the facts are suggestive of tax avoidance. Hence, the majority approach confirms the analysis presented earlier in this dissertation ("GST cases – the basic structure of interpretation").

The majority considered that this 'two step' approach resulted in the specific provisions and GAARs being complementary:[82]

> We consider Parliament's overall purpose is best served by construing specific tax provisions and the general anti-avoidance provisions so as to give appropriate effect to each. They are meant to work in tandem. Each provides a context which assists in

[81] at [130].

[82] at [103].

> determining the meaning and, in particular, the scope of the other. Neither should be regarded as overriding. Rather they work together.

The two step analysis therefore, according to the majority, reflects "Parliament's overall purpose".

Other principles of the judgment

It has been seen that the majority judgment reinforces the two step analysis propounded in this paper.

Other principles previously identified are also reinforced by the majority judgment.

Firstly, that once the legal nature of the transaction is ascertained, that status applies (and is a common approach) for contract law, land law and tax law. That the transaction should be treated the same is noted at pp 25 and 80 above.

The second principle is the majority's endorsement of the scheme and purpose approach when interpreting tax legislation (at p 82 above). In this respect, the majority confirm the emphasis on these factors as per *Databank*: see pp 27-33 above.

The third point is that English decisions provide limited direct assistance when New Zealand courts are interpreting domestic legislation. The majority stated that: "Care must, therefore, be taken when applying English cases in the different New Zealand context in which the meaning and scope of the [statutory] provisions must be

addressed and applied."[83] This also confirms the views previously identified in this paper (see p 30 above).

A fourth and important point is that the majority define the limit of the sham scenario. This has the effect of upholding the integrity of the legal form doctrine. They state:[84]

> The Commissioner argued that the insurance documents were a sham … A document will be a sham when it does not evidence the true common intention of the parties. They either intend to create different rights and obligations from those evidenced by the document or they do not intend to create any rights or obligations, whether of the kind evidenced by the document or at all …[W]e are of the view that despite what can be said about the insurance arrangements for avoidance purposes, the documents evidencing them did not misrepresent the nature of the rights and obligations which the parties to them intended to enter into … An allegation of sham, being akin to an allegation of fraud, should not be lightly made. Those engaging in a sham are in reality seeking to deceive others as to the true nature of what they have agreed and are intending to achieve.

It is to be noted that the Supreme Court upheld the validity of the legal form of the insurance contract despite the facts that the insurance company, CSI, had no office, telephone lines, employees or stationery.[85]

The final principles to be considered are those which relate to interpretation of GAARs. Of course, any worthwhile discussion of tax avoidance principles would

[83] at [110].

[84] at [32-39].

[85] at [134].

(at a bare minimum) comprise on its own a whole dissertation. Hence, the writer is conscious of being drawn into detailing such principles. She suffices with making two brief observations.

Firstly, that *Ben Nevis* involved a detailed consideration of the relevant anti-avoidance legislation (ss BG 1 and GB1 of the Income Tax Act). In 2000, the anti-avoidance provision in the GST Act (s 76) was rewritten to mirror the Income Tax Act provisions.[86] Hence, it can be argued that *Ben Nevis* would have direct application to the existing GST anti-avoidance provision. Indeed, it could even be argued that *Ben Nevis* is a leading authority on that provision (especially given that the Supreme Court decision in *Glenharrow*[87] is concerned with the pre-2000 GST provision).

Secondly, on occasions, the Privy Council has drawn a distinction between tax avoidance and tax mitigation.[88] Avoidance here means that no significant expenditure has been suffered by the taxpayer who is claiming a tax deduction (and the arrangement is therefore void for tax purposes). Tax mitigation, in contrast, arises where the deduction reduces but does not eliminate a tax liability and the deduction involves an actual and genuine expenditure (and is therefore permissible). The writer considers that this approach is consistent with the 'commercial reality' approach because tax mitigation involves an actual expense (or similar) being incurred, so that the economic or commercial cost would normally be consistent with the legal form. That is, the legal form and commercial/economic outcome will often match up (and therefore the transaction cannot be struck down for avoidance) in the circumstances of tax mitigation.

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[86] Inland Revenue Department Tax Information Bulletin Vol 12, No 12 (Dec 2000).

[87] *Glenharrow Holdings Ltd v C of IR* (2009), above n 43.

[88] *Peterson v C of I R*, above n 73; *Challenge Corporation v C of IR* [1986] 2 NZLR 513.

Concluding comments on the majority judgment

Overall, it is considered that majority approach in *Ben Nevis* represents a blueprint for the interpretation of anti-avoidance provisions, and arguably even a blueprint for courts to apply tax and other statute law.

It is considered that the approach of the courts to interpreting income tax legislation is the same approach that they take to interpreting any other piece of legislation (i.e. including GST legislation). This point has been made on several occasions by the House of Lords in an income tax context and has led it to state that:[89]

> *The paramount question is always one of interpretation of the particular statutory provision and its application to the facts of the case.*

Thus the *Ben Nevis* prescription arguably applies equally to GST. As such, it not only illustrates how the 'traditional purposive approach' works, but it substantially validates the analysis undertaken earlier in this paper.

Minority judgment analysis

The approach of the minority is considered briefly below. While they reached the same conclusion as the majority, they adopted a different approach as regards step one of the two step analysis. The majority described the minority's approach as the "more purposive approach".[90]

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[89] *MacNiven v Westmorland Investments Ltd* and *Barclays Mercantile Business Finance Ltd v Mawson (HM Inspector of Taxes*) as per n 9 above.

[90] at [110].

This approach has been used in some recent English cases, and the minority considered that there should be no difference between the general approach to statutory interpretation of specific tax provisions in New Zealand and in the United Kingdom.

The minority state that:[91]

> In a fiscal statute the terms and concepts used may, depending on purpose and context, be used in a business or accounting sense. It will be wrong to start with any preconception that 'ordinary meaning' or 'legal meaning' is to be preferred to the meaning a term has in business or accounting. Similarly, where the substance of an arrangement needs to be gauged in application of the provision of a tax statute, a purposive construction of the provision may indicate that it is legal substance which is in issue or it may indicate that the statute is concerned with business substance.

The justices do *not* accept that before considering the question of tax avoidance, when considering the application of the specific provision, "the Court is concerned primarily with the legal structures and obligations created by the parties, and not with the economic substance of what they do". Hence, whether legal or economic substance prevails "depends on the context."[92]

The majority are therefore wrong to assert that the first step is to examine the legal rights and obligations that the parties have entered into. Rather, whether the facts (to which the specific legislation is to be applied) are analysed with reference to legal status or business substance, depends on the purpose and context of the legislation.

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[91] at [4].

[92] at [5].

So for income tax, which is a commercial piece of legislation, the analysis of the facts will often be according to business principles rather than legal status of the transaction.

The difference in this approach is illustrated by the licence premium issue in *Ben Nevis*. The minority considers that the deduction would only arise if the expense was "incurred" in ordinary commercial terms (because the purpose and context of the deduction provision requires the application of commercial terms). The promissory notes used to effect payment were artificial devices and, commercially, did not comprise incurred expenditure. Accordingly, they did not generate a deduction under the relevant specific provision.

The minority accept what Lord Cooke has argued for in the case of *McGuckian*[93] about the relationship between the specific provisions and general anti-avoidance provisions. He has described a purposive approach to the construction of specific tax provisions as being "antecedent to or collateral with … general anti-avoidance provisions such as are found in Australasia."[94]

This is to say that it is antecedent if the arrangement does not come within the purpose of the specific provisions, then the approach will be to stop at the first step where the deduction is not allowed, and it will not go on to the second step.

It is collateral, if the arrangement aims to defeat the purpose of the specific provisions. Here, a tax avoidance issue is raised, and there will be a second step to invoke the general anti-avoidance provision.

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[93] *Commissioners v McGuckian* [1997] 1 WLR 991.

[94] at [7].

As can be seen, the ‘more purposive approach’ used by the minority justices is quite different from what the majority justices used.

Under the ‘traditional purposive approach’ used by the majority, no matter what is the purpose of the legislation itself, the starting point is to examine the legal status of the transaction, and then to apply the specific provisions. The more purposive approach advocates using the purpose and context of the legislation to measure the facts, before applying the specific provision to those facts. Then, if there is a tax avoidance issue involved, both approaches move on to the second step, which is to invoke the general anti-avoidance provision.

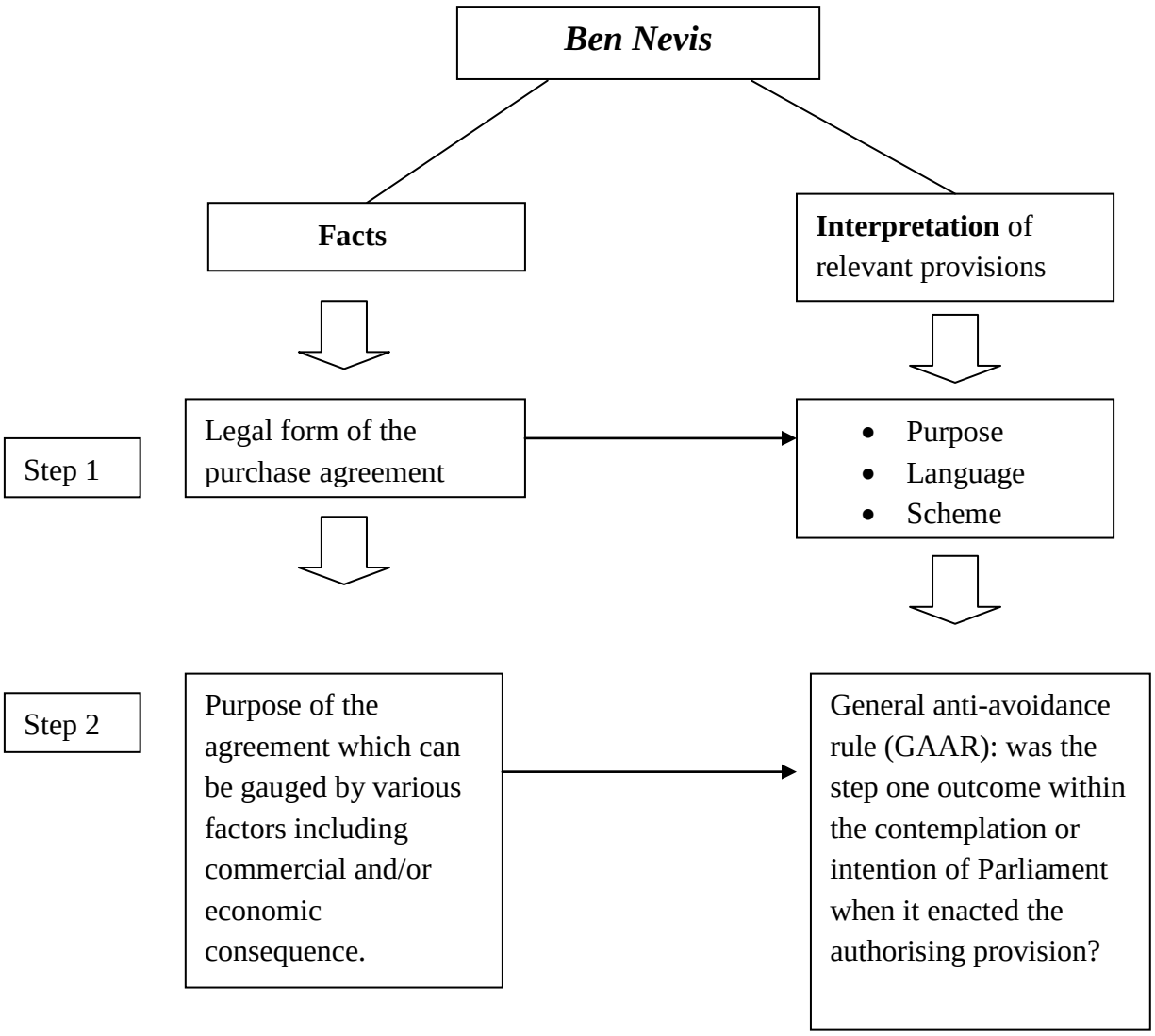
Consistency with GST principles

The approach of the majority in *Ben Nevis* has reinforced the approach of *Databank*. In *Databank*, Lord Templeman undertook an analysis of the legal obligations entered into and carried out in order to ascertain the facts of the case. He then applied the specific provisions of the GST Act to those facts.

This is the same approach advocated (and applied) by the majority in *Ben Nevis*.

The approach of both the majority and the minority in *Ben Nevis*, confirms the extra leg approach used in *Glenharrow*. All judges in both cases considered that there needed to be a second step (the extra leg) when a case is suggestive of tax avoidance. The facts here can be measured objectively with reference to commercial or economic yardsticks (or similar). Tax avoidance exists if the commercial or economic outcome (of the arrangement) is outside the purpose and contemplation of the relevant statutory provision.

Diagram


Ben Nevis
Facts
Interpretation of relevant provisions
Step 1
Legal form of the purchase agreement
Purpose
Language
Scheme
Step 2
Purpose of the agreement which can be gauged by various factors including commercial and/or economic consequence.
General anti-avoidance rule (GAAR): was the step one outcome within the contemplation or intention of Parliament when it enacted the authorising provision?

Principles extracted from the above cases

The writer has set out below the principles previously identified in this paper arising from the GST cases. Given that they are derived from leading decisions of New Zealand's highest court, the principles provide authoritative guidance on the interpretation and application of the GST Act. Accordingly, the writer considers that they provide a tangible framework for persons who are interpreting the GST Act, or are reading GST case law. It is conceivable that they could even provide assistance to overseas people studying New Zealand GST with the intention of adopting a similar regime in their country.

The cases which support each principle are also identified. The writer has taken the liberty of including *Ben Nevis* as a further confirming authority for some of the principles extracted from the GST cases.

Key Principles

The key principles collected from the leading cases are set out below.

- When ascertaining the relevant facts, it is appropriate to examine the legal arrangements entered into and carried out (*Databank; Glenharrow; Ben Nevis*).

- When interpreting the GST Act, the courts primarily examine purpose, scheme and language (*Databank; Glenharrow; Ben Nevis*).

- The scheme of the GST Act is "transaction based" and therefore each transaction has to be analysed separately (*Databank*).

- A two stage process is used for interpreting documents: the first stage is to determine the legal rights and obligations which the parties have entered into and carried out, and the second is to classify those rights and obligations at law (*Agnew*).

- On occasions, facts are not ascertained by reference to legal form. This is the case where the statutory provision does not require an examination of the legal nature of the transaction (*Kena Kena; Edgewater*). This "exception" apparently more readily applies if a case is not concerned with an imposition issue (*Kena Kena; Edgewater*).

- In circumstances where a tax avoidance issue is involved, an 'extra leg' is added to the approach. This calls for an objective assessment of the purpose of the arrangement, and then ascertaining whether the economic consequence or broad substance of that arrangement produces an outcome contemplated by Parliament (*Glenharrow; Ben Nevis*).

Further principles of facts

Further principles are advocated in the cases on ascertaining the facts of the case. They are included in the below bullet point.

- When ascertaining facts, a form over substance approach normally applies as opposed to a substance over form approach (*Databank; Agnew; Glenharrow; Ben Nevis*). However, when ascertaining facts for tax avoidance purposes, a commercial or economic yardstick can be applied to measure the purpose of the relevant arrangement (*Glenharrow; Ben Nevis*).

The writer notes that the usual form over substance approach is further reinforced by two principles expounded in *Ben Nevis*. Firstly, that a determination of legal form applies not only for taxation purposes, but applies equally to other areas of law such as contract and land law (unless there is statutory direction to the contrary). That is, the legal status of the transaction is also significant because it applies across all areas of common law. Secondly, that the application of the sham doctrine is limited; thereby according wide application to legal form. See further pp 85-86 above.

Further principles of interpretation

The cases have also identified supplementary interpretation principles, or can be read as suggesting such principles. These principles are collected together below.

- The GST Act and other fiscal legislation are interpreted in the same manner as other statutes (*Databank*).

- The 'scheme' of the GST Act apparently applies readily when the statutory direction is concerned with the quality of the "supply" (such as is usually the case with Part II of the Act, "Imposition of Tax"). It might not apply so readily to other Parts of the Act. (This contention of the writer is based on her reading and consideration of *Databank* and the other cases.)

- For GST 'imposition' cases, the analysis of scheme seems to be more influential than the analysis of the purpose and language of the Act. (The writer's contention here is based on her reading and consideration of *Databank* and the other cases.)

- Overseas VAT and GST cases have limited application to New Zealand GST given the differing language and scheme of the legislation (*Databank; Ben Nevis*).

- Further interpretation principles apply in relation to the application of GAARs. Perhaps the most prominent for GST avoidance cases, is that the analysis of the 'purpose' of the Act - or what was 'within Parliament's contemplation' - is more important than the analysis of the scheme and language of the Act. If the intention of the arrangement is aimed to defeat the purpose of the Act, then the GAARs will normally be invoked (*Glenharrow; Ben Nevis*).

Conclusion

Summary

This dissertation has explored decisions of the Privy Council and Supreme Court on the GST Act. It details and analyses five leading GST cases. It identifies and collects together interpretation principles from those cases, and proceeds to test those principles against the leading income tax decision of the Supreme Court, *Ben Nevis*.

There is an overall trend. The first case, *Databank*, provides founding principles. Namely, that facts are ascertained by the legal nature of the transaction and the specific statutory provisions are then applied with reference to their wording and the purpose and scheme of the Act. This is termed the 'traditional purposive approach'. The emphasis on determining facts with reference to the legal relations entered into is further confirmed and explained in *Agnew*.

Subsequent cases establish both an exception and an addition to this traditional purposive approach.

The exception apparently arises where the statute directs the factual enquiry to other than the legal nature of the underlying transaction. The exception applies, for example, where the statutory enquiry concerns whether the payer pays a "subsidy" (*Kena Kena*) and to the order of the priorities for a company which is in receivership (*Edgewater*).

The addition arises where the facts are suggestive of tax avoidance. Here, the 'extra leg' examines whether the purpose of the arrangement (which can be measured objectively via a commercial or economic yardstick) was within the contemplation

of Parliament when the specific authorising provision was enacted (*Glenharrow; Ben Nevis*).

The very basis of the 'traditional purposive approach' has recently been questioned judicially. Recent English cases favour a 'more purposive approach'. This entails ascertaining the nature of the statute (commercial or otherwise) as a starting point, and then interpreting the facts of the case accordingly (eg, usually commercially rather than via legal form in the case of a commercial statute).

The minority in *Ben Nevis* expressively endorsed this more purposive approach. However the majority in *Ben Nevis*, and whole of the Supreme Court in *Glenharrow*, applied the traditional purposive approach. Hence, the *Databank* type of approach has been upheld (in the last 15 months) by the Supreme Court in both a GST and an income tax context. Both of these recent Supreme Court decisions also upheld the addition of the 'extra leg' second step.

Accordingly, the two step approach to interpreting the GST Act advocated in this dissertation reflects settled law. Similar status applies to the exception to step one of the 'traditional purposive approach'.

Conclusion

The conclusion of the dissertation is therefore that there is a defined 'model' of the courts interpretation of the GST Act.

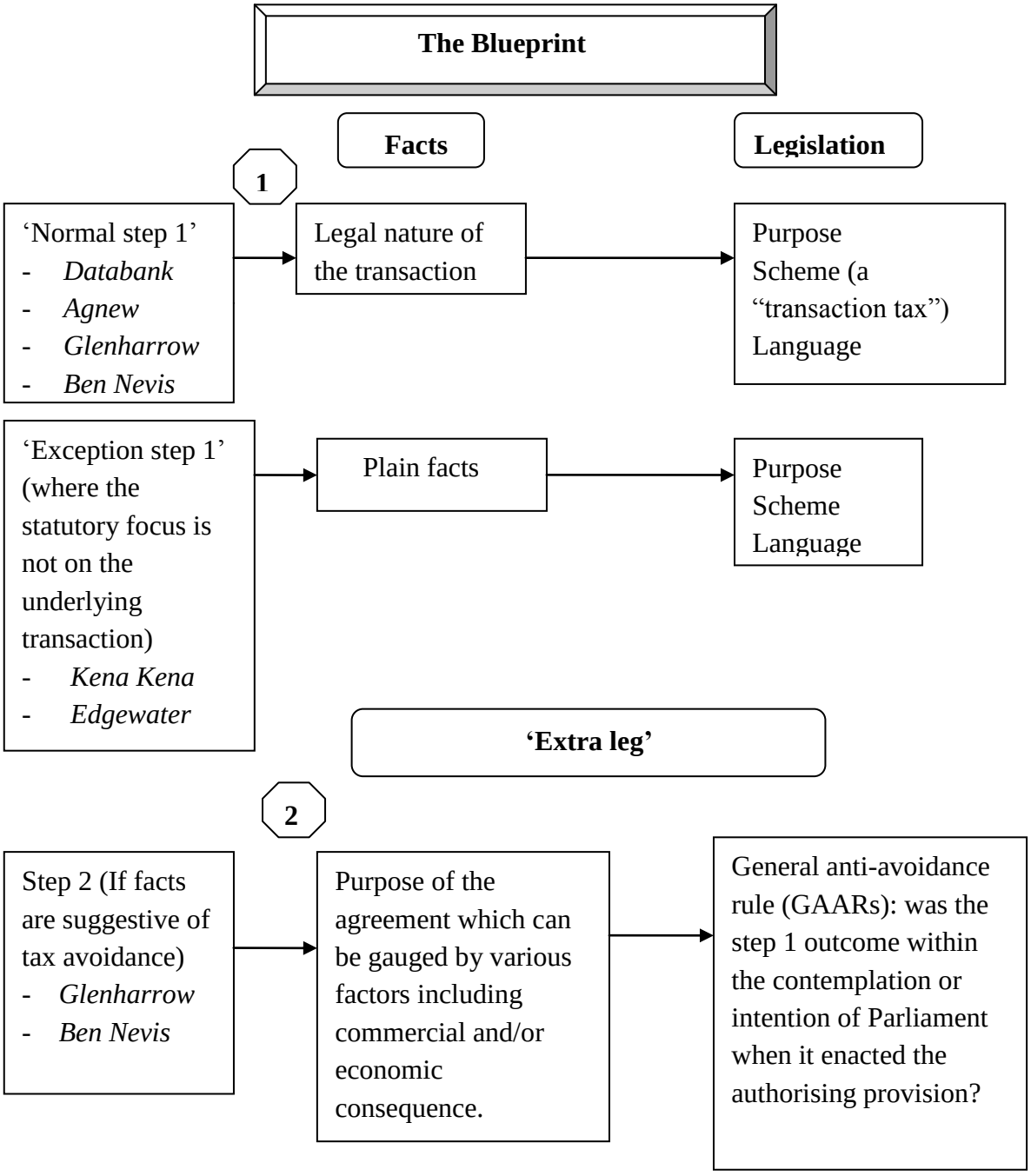
This assertion, can of course, be challenged. The primary challenge would be that the conclusion is based on insufficient data, viz five GST cases and one income tax case. However, as outlined in the summary above, the force and weight of those six

cases (in the writer's opinion) place the status of the model beyond doubt. It would also be possible to 'test' this model against a wider range of GST cases, and the author recommends that further work be undertaken in this respect, including reviewing leading Court of Appeal and High Court cases to further scrutinise the model.

However, it is her view that given its recent endorsement by New Zealand's highest court, the model will continue to serve for the interpretation of the New Zealand GST Act for the foreseeable future.

Additional principles of factual and legislative interpretation supplement the model. These have been listed on pp 93-96 above. The very heart of this dissertation, however, is the identification of the following model or 'blueprint' for the interpretation of the GST Act.

Diagram – Blueprint for the interpretation of GST Act



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