



WEEKLY COMMENT: FRIDAY 18 APRIL 2014

1. Last week I looked at the GST grouping rule in s. 55(8) of the *Goods and Services Tax Act 1985* ("the GST Act"), which applies when not all of the persons in the GST group are companies. This week I will look at the implications for this grouping rule of stated views of Inland Revenue and the TRA on the meaning of common control as expressed in:
 - (a) Inland Revenue QWBA QB 07/03 *Trustees in the context of the Goods and Services Tax Act 1985: does a separate trustee capacity and personal capacity exist and do separate trustee capacities exist for trustees of multiple trusts?* (June 2007); and
 - (b) *Case 11/2013* [2013] NZTRA 11, (2013) 26 NZTC 2-010.
2. It is worth re-stating the rule in s. 55(8): The Commissioner can deem a group of registered persons to be members of a GST group, and the rules that apply to groups of companies in sections 55(2) to 55(7) will apply as if the group of registered persons is a group of companies, and as if references to companies are references to members of the group, if the Commissioner is satisfied in relation to 2 or more registered persons (not each being companies) that:
 - (a) One of them controls each of the others; or
 - (b) One person controls all of them; or
 - (c) Two or more persons carrying on a taxable activity in partnership control all of them.
3. QB 07/03 and *Case 11/2013* concerned whether trusts and companies respectively were associated persons, and they contain relevant discussions on the meaning of common control.

QB 07/03: Separate trustee capacities

4. QB 07/03 concerns Inland Revenue's position on whether, in the context of the "associated persons" definition in s. 2A(1) of the GST Act, a person acting in their capacity as a trustee of a trust is acting in a different capacity from when they are acting in their personal capacity. A related question is whether a person who is a trustee of more than one trust is to be regarded as possessing a separate trustee capacity for each particular trust.
5. The answer is that for the purposes of the "associated persons" definition in s. 2A(1) of the GST Act, a person acting in their capacity as trustee of a particular trust will be treated as acting in a different capacity from when they are acting in their personal capacity. A person who is a trustee of more than one trust is to be regarded as possessing a separate trustee capacity for each particular trust.

6. The definition of "trustee" in the GST Act is an inclusive definition as it states that "trustee" includes an executor and administrator. It is stated in QB 07/03 that by using an inclusive definition, Parliament must have intended to also rely on the common law meaning of "trustee". Case law recognises that a person acting in their capacity as a trustee of a trust is acting in a different capacity from when they are acting in their personal capacity.
7. QB 07/03 underlines the difficulty in trying to obtain group registration for different trusts. However, the example included in QB 07/03 clearly indicates that a person may be associated with a trustee through being a person who has benefited or is eligible to benefit under the trust. Commonality of beneficial interests linked through the terms of the trust deeds could provide a basis for group registration – as in example 3 in the TIB item *GST Group Registration Of Trusts* discussed in last week's *Weekly Comment*.

Case 11/2013

8. This case is particularly interesting because the Commissioner successfully argued that control through a corporate trustee of a company that was a trust asset constituted control "by any other means whatsoever", which was sufficient to create an association with another company that was not held through the trust. The case provides a basis for GST group registration in similar circumstances.
9. The taxpayer company bought a property from another company. The seller was not GST-registered. The seller had acquired the property earlier for \$847,000, including GST of \$94,111.12. Before the sale the seller incurred additional costs in developing the property, so that by the time of the sale the seller had spent \$3,009,296.
10. The selling price was \$8,034,750, which was paid by way of book entry. The taxpayer – the buyer company - claimed input tax deductions in respect of the price paid. The deductions were disallowed because the Commissioner maintained the seller and buyer companies were associated under s. 2A(1)(a)(iii) of the GST Act. Therefore, the input tax deduction was limited to \$94,112.12, which was the GST paid by the seller upon the original acquisition of the property.
11. The seller was a company that was held in trust. The holder was a trustee company, which owned all the shares in the seller. The same individual held all the shares in the trustee company and all the shares in the buyer company. The individual was also the sole director of both companies.
12. The question before the TRA was whether the seller and buyer companies were associated under s. 2A(1)(a)(iii) of the GST Act because the same person "had control of each of those companies by any other means whatsoever".
13. It was acknowledged that the companies could not be associated under s. 2A(1)(a)(i) because the individual did not hold 50% or more of the voting interest in both companies. This was because of the existence of the trust. The trust owned the voting interest in the seller. The Commissioner accepted that the beneficial ownership of the seller company's shares had been separated from the legal ownership, which altered the capacity in which the trustee company held the shares and made them trust property. As a result, there was no commonality between the buyer and the seller through the shares held by the individual in the buyer and the trustee company.
14. The taxpayer – the buyer company - contended that:

- (a) The individual controlled the buyer company and the trustee company (which owned the shares in the seller) through his voting interest, whereas the use of the words “other means” in s. 2A(1)(a)(iii) required the control, for the purposes of s. 2A(1)(a)(iii), to be exercised in some way other than the voting interest control referred to in s. 2A(1)(a)(i);
- (b) Because control by voting interests is dealt with in s. 2A(1)(a)(i) and (ii), control by voting interests should be excluded in s. 2A(1)(a)(iii), because the control should be by means other than those identified in the earlier subparagraphs;
- (c) The taxpayer and the Commissioner had both relied on QB 07/03 to exclude association based on s. 2A(1)(a)(i), because the corporate trustee acts in a capacity as trustee and, therefore, could not be associated with the individual other than in its own (non-trustee) capacity: there could be no sensible reason to exclude association under s. 2A(1)(a)(i) due to the existence of the trust, and yet not exclude association under s. 2A(1)(a)(iii);
- (d) Officials have stated, and the taxpayer accepted, that s. 2A(1)(a)(iii) is in the nature of a “back stop” to the primary voting interest test, but the taxpayer considered that control by any other means applied when:
 - (i) Voting power is in the hands of persons who are subservient to another person (following *Himley Estates Limited v Commrs of Inland Revenue* [1933] 1 KB 472); or
 - (ii) Control could not be resolved as a matter of law and de facto control had to be considered;
- (e) The use of the word “each” meant both the buyer and seller companies had to be controlled in the same way – i.e. the same test of association under s. 2A(1)(a)(iii) applied to both companies.

15. The Commissioner contended that:

- (a) The language of “control” in relation to companies has predominantly been held to mean legal control, although control as a matter of fact may be relevant depending upon the context (following *Case K54* [1988] NZTRA 40, (1988) 10 NZTC 444);
- (b) The Courts have generally rejected the argument that control is linked to the beneficial interest held in the company (following *British American Tobacco Company Limited v Inland Revenue Commissioners* [1943] AC 335 (HL)): the controlling interest is held by the person who has the requisite voting power;
- (c) The argument that shareholders did not have a “controlling interest” in the company because they held the shares on trust was rejected in *Inland Revenue Commissioners v J Bibby and Sons Limited* [1945] 1 All ER 667 (HL);
- (d) There is no sound policy reason why legal control by shareholding should be excluded from the ambit of s. 2A(1)(a)(iii), and a finding that a person does not control a company where he owns 100% of the shares (and where he is also the sole director) would be contrary to well established authority;
- (e) Because control of a company via a corporate trustee does not come under s. 2A(1)(a)(i) it must be by “other” means under s. 2A(1)(a)(iii), as the alternative is an artificial limitation on the scope of this subparagraph that is at odds with the intention of the Legislature;

(f) Section 3A(3)(a) was introduced to counteract the “mischief” where the on supply of goods to an associated company was being used to obtain an input tax deduction which would not have been available if there had been no on-supply, and s. 2A(1)(a)(iii) should be interpreted having regard to the purpose of that provision.

16. Judge Sinclair ruled as follows:

(a) The language of “control” in relation to companies has predominantly been held to mean legal control, although control as a matter of fact may be relevant depending on the context. In this case it is not in issue that the individual had legal control of each of the companies through voting interests.

(b) Section 2A(1)(a)(iii) is wide enough to encompass forms of control other than when voting power is in the hands of persons who are subservient to another person.

(c) In *IRC v Bibby* the Court held that the fact that a shareholder was a trustee was not a relevant consideration when determining legal control. Accordingly while it is a relevant consideration under s. 2A(1)(a)(i), the existence of the trust is not a matter to be taken into account under s. 2A(1)(a)(iii).

(d) The use of the phrase “by any other means whatsoever” supports the Commissioner’s contention that s. 2A(1)(a)(iii) is intended to have wide effect and to operate as a “catch all” test to cover association of companies by control not specifically covered by the tests under s. 2A(1)(a)(i) and (ii).

(e) It follows that control via a corporate trustee must be by “other means” and come within s. 2A(1)(a)(iii).

(f) There would appear to be no policy reason why control by voting interests should not be included under s. 2A(1)(a)(iii). Section 3A(3)(a) of the GST Act was introduced to address the situation where second-hand goods are sold to an associated person principally to gain the input tax credit. If the limited interpretation of s. 2A(1)(a)(iii) is adopted the effect would be to exclude companies which would clearly have been associated under s. 2A(1)(a)(i) except for the involvement of a corporate trustee, and that was not the intention of the Legislature.

(g) Accepting the taxpayer’s argument that s. 2A(1)(a)(iii) implied that the method of control should be the same for both of the companies would unduly restrict the application of the subsection.

17. There was an additional argument put forward by the Commissioner following the decision in *RWR v AJR (Trusts)* [2010] NZFLR 82 (HC). The Commissioner submitted that the individual also had control of the seller company because he controlled the trust. He had full control of the sole trustee, which had capacity to appoint beneficiaries. In his personal capacity, he had the power to appoint or remove the trustees.

18. In *RWR v AJR* the trust deed gave RWR as settlor the power to appoint a new trustee. The trustee appointed by him was a company of which he was the sole director and sole shareholder. The High Court concluded that the combined effect of these two factors was that RWR had control over the trust. The Commissioner submitted that the individual had control over the trust in the same way.

19. The judge noted that the case of *RWR v AJR* was a relationship property case and was focused on different issues. Due to the finding that the companies were associated through the individual's legal control, it was not necessary to consider the question of control over the trust.
20. The case lends authority for group registration of companies controlled through different trusts, and possibly also different trusts controlled by the same corporate trustee with other features suggesting control over the trusts.



Arun David, Director
DavidCo Limited