TAXATION REVIEW AUTHORITY

TRA 43/11

[2013] NZTRA 10

IN THE MATTER OF	the Income Tax Act 2007 and the Tax Administration Act 1994
BETWEEN	[redacted] Disputant
AND	THE COMMISSIONER OF INLAND REVENUE Defendant

Hearing: 2 & 3 July 2013

Appearances: J Coleman for the Disputant
D Lemmon and Ms L Herbert for the Defendant

Decision: 5 December 2013

RESERVED DECISION OF JUDGE AA SINCLAIR AS TAXATION REVIEW AUTHORITY

ISSUES

[1] The issues arising in this proceeding are:

(a) whether the disputant was a New Zealand tax resident for the income tax years ending 31 March 2004, 31 March 2005, 31 March 2006 and 31 March 2007; and

(b) if so, whether the shortfall penalties for taking an unacceptable tax position apply under s 141B of the Tax Administration Act 1994 (the TAA) for each of the tax years in question.

[2] If it is found that the disputant is a New Zealand tax resident then a further issue arises as to the correct quanta of the assessments in the relevant years. By consent, this issue has been adjourned pending the outcome of this hearing.

[3] The dispute covers the tax years 31 March 2004 to 31 March 2007 so that the relevant legislation is the ITA 1994 and ITA 2004. The relevant provision in each Act is s OE1. These two provisions are identical in material respects. The Commissioner accepts that the disputant was personally absent from New Zealand for the requisite 325 day period under s OE1(3) and is therefore deemed to be a non-resident by virtue of the operation of that section in each of the relevant tax years. The Commissioner however relies upon s OE1 (1) and submits that the disputant is still a New Zealand tax resident by virtue of having a permanent place of abode in New Zealand. It is the disputant's contention that he did not have a permanent place of abode in New Zealand in the tax years in question.

[4] With regard to the imposition of shortfall penalties, the Commissioner submits that viewed objectively, the disputant is liable to pay shortfall penalties for taking an unacceptable position in his 2004 – 2007 tax returns. The disputant contends that the shortfall penalties are incorrectly imposed.

[5] The onus of proof is on the disputant while the standard of proof is the balance of probabilities.[1]

FACTUAL BACKGROUND

[6] Evidence was given by the disputant, his former wife AB and by the disputant's former brother-in-law. Much of the brother-in-law's evidence was hearsay and it was apparent that he had little personal knowledge of the couple's relationship. The evidence of the disputant and AB was largely consistent and overall I found them both to be credible witnesses.

[7] The disputant was born in New Zealand. He joined the New Zealand Army as an electrical and mechanical engineer in 1978. He served for 25½ years both in New

[1] S 149A TAA

Zealand and overseas before retiring in June 2003. The disputant was married to AB in May 1981. The couple separated in August 1994. At that time, AB was pregnant with the couple's fourth child. Following the separation AB moved to a provincial town with the children and purchased a house. In 1996 AB wanted to purchase a larger property but she was in receipt of the Domestic Purposes Benefit and did not have the financial means. The disputant agreed to put his name on the Certificate of Title so that AB could obtain a mortgage. AB subsequently purchased a property at 24 J Esplanade (the Esplanade property) and the disputant contributed to the mortgage payments in lieu of paying child support.

[8] In 1998 AB wanted to purchase another property. The disputant agreed to buy AB's share in the Esplanade property and again agreed to his name going on the Certificate of Title to assist AB's mortgage application. AB purchased a house at 79 M Road. The disputant never made any contribution to the mortgage payments for this property. After 1998 the Esplanade property was rented on a periodic tenancy basis.

[9] Following his retirement from the Army the disputant went to Papua New Guinea in July 2003 and worked for an overseas aid agency on a 12 month contract. His principal role was to provide security for the agency's personnel. From July 2004 until October 2004 the disputant was in Queensland. He holidayed during this time and also worked for a scrap metal merchant for about a month. His income from this employment was paid into a bank account which he opened in Queensland.

[10] On 26 October 2004 the disputant started work in Iraq for an American security company as a member of its personal security detail team. He was employed on a 13 month contract which he was able to apply to renew. The disputant's contract was renewed on a number of occasions over subsequent years. In about 2011 the disputant went to work for another security company in Iraq before leaving the country in April 2012. The disputant then moved to Australia and began work for an engineering company in Mount Isa.

[11] The disputant gave evidence that when he left New Zealand in July 2003 he had no intention of returning to this country to live. His intention was to continue

working in the hot spots around the world as long as he could and when he was no longer able to work as a security consultant, he intended to buy a house in Australia and settle there.

[12] While living in Iraq, the disputant lived at three addresses. The first address was a hotel which was fortified and protected around the clock by security personal. The other two addresses were fortified compounds also with around the clock security. Because of safety issues, the disputant spent his leisure time within the compound.

[13] The disputant's salary from his first employer in Iraq was paid in US dollars into a Fort Worth, Texas bank account.[2] The Fort Worth account could be accessed by a debit card. The disputant gave a card to AB so that she could withdraw funds to meet mortgage payments and other expenses relating to the disputant's property assets (discussed below) and to pay child support of $2,000 a month and other expenses (eg dental, dancing and school fees, car repairs and presents) for the children. The disputant told the Authority that he was not aware of all the individual withdrawals. AB would phone or email him if she was going to take out large amounts of money and he stated that he had no problem with this arrangement. AB told the Authority that she had access to the card up until about March 2011 and in that period the amounts taken out by her in relation to the disputant's property interests totalled $245,253.98 while those in relation to the children's expenses (excluding the agreed child support and presents) totalled $94,861.27.

[14] The couple's eldest daughter also had access to the account to assist paying her expenses when she was living in England in 2004 - 2005. As well, money was stolen from the account by one of the disputant's sons and a girlfriend who obtained details of the account number. The amount taken was around $20,000 in total. Most of those funds were later recovered.

[15] As part of his employment, the disputant was provided with food and accommodation in Bagdad so that he spent very little money in that country. The

[2] The disputant gave evidence as to his income in the relevant tax years. The Commissioner has assessed the income earned by the disputant in each year as being more and these assessments are in dispute.

amounts which he withdrew from the Fort Worth account were spent on travel and holidays out of Iraq. The salary received from the disputant's second employer in Iraq was paid into the disputant's bank account in Australia.

[16] It was the disputant's evidence that he visited New Zealand about every 5 - 6 months. In the tax years in question the disputant spent a total of 168 days in New Zealand being an average of 42 days per tax year[3]. When the disputant visited New Zealand he would stay with AB for between two to five days to see the children. After that, he visited his mother and other family and friends. When he was in Iraq the disputant endeavoured to ring his children every Sunday night. This was not always possible depending on work commitments and communications. As well he also had holidays with the children in France, England, Turkey, Australia (three times) and Fiji.

[17] In 2006 the disputant went to the Gallipoli commemorations in Turkey where he arranged to meet his eldest daughter. While there he met a New Zealand woman with whom he had a relationship. The relationship continued during the disputant's subsequent visit to New Zealand. A child was born but the relationship did not last. The disputant also made periodic payments to the woman as maintenance for his daughter. AB withdrew funds for that purpose from the Fort Worth bank account and arranged payment. On occasion the disputant also visited his young daughter when he was in New Zealand.

[18] The disputant nominated AB as his emergency contact under his employment contract in Iraq. He also used AB's address at 79 M Road as his address on arrival and departure cards and Companies Office records. In December 2006 on a visit to New Zealand the disputant granted AB enduring Powers of Attorney in relation to his property and for his personal care and welfare.

[19] In 2000 AB formed a partnership with the disputant to own rental properties. On advice she subsequently incorporated Company X in June 2005. AB holds 99 of the 100 shares in this company and the disputant holds the remaining 1 share.

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[3] In the years 2008 to 2011 this increased to an average of 51 days per year.

Company X was set up as an LAQC and the shareholding structure enabled AB to claim the tax losses against her personal income.

[20] The directors of Company X are AB and the disputant. AB was (and continues to be) responsible for all aspects of running the rental property business. The following rental properties were transferred to Company X or subsequently purchased:

(i) the Esplanade property
(ii) 1 Y Street[4]
(iii) 31 P Road
(iv) 2 S Drive[5]

Three of these properties (including the Esplanade property) are located in the provincial town where AB lives and the fourth property is located in another town in close proximity. Both the disputant and AB gave evidence that the disputant is the beneficial owner of the Esplanade property and of a half share in 2 S Drive while AB beneficially owns 1 Y Street, 31 P Road and a half share in 2 S Drive.

[21] In April 2005 the disputant also purchased two blocks of bare land in New Zealand. One block is in close proximity to the provincial town while the other is located further north. The Authority heard that AB's name is also on the title of those two blocks because all lending in respect of the properties owned by the disputant, AB and Company X is cross guaranteed.

[22] The disputant's name also appears together with that of AB, on a property owned by AB's brother and sister-in-law. Neither the disputant nor AB have any beneficial interest in this property. As well the disputant also inherited an interest in two blocks of Maori land.

[23] In her evidence AB observed that the disputant was not very financially literate. He had spent the superannuation money that he had received from the Army in 1998 with nothing to show for it apart from buying AB's half of the Esplanade property. AB told the Authority that she had recommended that the disputant buy

[4] Previously owned by the disputant's eldest daughter and transferred to Company X in December 2008
[5] Transferred from the property rental partnership

the two blocks of land to put his money into and had become in effect, his financial advisor.

[24] The disputant filed tax returns for the 2004 and 2005 tax years signed by AB on his behalf. The income returned in each case was the rental income earned on the Esplanade property and rental property partnership while partnership and other losses were claimed. The question on the forms as to being a non resident for tax purposes was unanswered and no overseas income was disclosed. In December 2007 following the commencement of the Inland Revenue investigation, AB signed a New Zealand tax residence questionnaire on behalf of the disputant. The question as to accommodation in New Zealand was answered by the notation "see other factors". Under that heading was stated:

> [The disputant] has no permanent place of abode in NZ and when he returns to NZ for short periods of time, he divides his time of stay with his brothers or mother, or his ex-wife [AB] and their children.
>
> [The disputant] has a 1% shareholding in [Company X] which owns three rental properties. This company has made losses to date.

[25] The disputant told the Authority that while he and AB did not live together as husband and wife following their separation in 1994 it was not until March 2009 that a Separation and Relationship Property Agreement was signed and the marriage was formally dissolved. In the same month the disputant also executed a will appointing AB as his sole executor and trustee.

[26] The Separation Agreement provided that Company X was to continue. There was no particular mention of the properties owned by that company but the disputant and AB were both adamant that the disputant continues to be the beneficial owner of the Esplanade property and of a half share in 2 S Drive. The Separation Agreement provided for the transfer of 79 M Road to AB and for the transfer of the bare blocks of land to the disputant. Because of the extent of the borrowing and AB's limited earning ability, the bank has not permitted these transfers to be completed.

[27] As well as the assets referred to above, the disputant has in New Zealand a superannuation fund which will provide him with an income at 60 years old and a

life insurance policy. His only bank accounts in this country were for the purpose of mortgage payments and he did not operate a credit card.

[28] At the time of his departure from New Zealand the disputant also had four motor vehicles and a motorbike registered in his name. The BMW had been purchased by the disputant's brother-in-law but in view of his financial position the car was registered in the disputant's name. The brother-in-law failed to make the loan payments and the disputant took over responsibility for doing so. This occurred after the disputant left New Zealand. AB gave evidence that the disputant never drove the car and in 2005 it was transferred into her name. Repairs were undertaken on the vehicle and it was subsequently sold. The 1992 Isuzu station wagon was the disputant's vehicle. He gave it to AB when he left New Zealand. In 2004 – 2005, the motor blew up and the car was scraped. The disputant purchased the Honda motor bike in 1996. He left this bike with AB. It was AB's evidence that it did not go and it was still at her home. The other two vehicles belonged to AB and to the disputant's eldest daughter.

[29] AB told the Authority that the disputant's relationship with his children deteriorated over the years as a consequence of his absence from New Zealand and the limited time he spent with the children on his visits. As the children got older she had given up trying to maintain the relationship. It was AB's evidence that the disputant no longer contacts the children and in recent years the two youngest children had both obtained special study link allowances on the basis that they had no relationship with their father.

LEGAL ISSUES

[30] Section OE1(1) of the ITA 1994 and the ITA 2004 provides that:

> Notwithstanding any other provision of this section, a person, other than a company, is resident in New Zealand within the meaning of this Act if that person has a permanent place of abode in New Zealand, whether or not that person also has a permanent place of abode outside New Zealand.

[31] The phrase "permanent place of abode" has not been defined in the legislation. The issue has been considered in a number of cases which provide some guidance as to the factors to be taken into consideration in determining whether a

person has a permanent place of abode in New Zealand. The test of whether a person has a permanent place of abode is an objective test.[6] It is to be determined as a matter of fact taking into account the totality of the circumstances.[7]

[32] A permanent place of abode is one which is lasting or enduring as opposed to temporary.[8] The person's intention as to length of stay is material but it is not determinative.[9] An intention to stay outside New Zealand is not inconsistent with having a permanent place of abode in New Zealand.[10]

[33] In *Case Q55* Judge Barber provided a non-exhaustive list of factors to be considered in determining whether a person's permanent place of abode is in New Zealand. He stated:[11]

> The cases show that determination of whether the objector's permanent place of abode is in New Zealand depends on such considerations as the following:
>
> (a) Reasons for going overseas;
> (b) Whether the objector established a permanent place of abode out of New Zealand;
> (c) Arrangements made by the objector concerning his home in New Zealand;
> (d) Employment;
> (e) Financial ties with New Zealand;
> (f) Other ties with New Zealand;
> (g) Length of time out of New Zealand.

[34] In *Case Q55* Judge Barber also considered what was required to have a "permanent place of abode". He stated:[12]

> I consider that "has a permanent place to abode" does not require that a dwelling be always vacant and available for the taxpayer to live in; but that there is a dwelling in New Zealand which will be available to the taxpayer as a home when, and if, that taxpayer needs it, and that the taxpayer intends to

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[6] *Case H97* (1986) 8 NZTC 664, *Case J 98* (1987) 9 NZTC 1,555, *Case Q55* (1998) 15 NZTC 5,313; *Federal Commissioner of Taxation v Applegate* (1979) 27 A 114 (FCA)
[7] *Case F139* (1984) NZTC 60,245; *Federal Commissioner of Taxation v Applegate* (1979) 27 ALR 114(FCA); and *Case H97* (1986) 8 NZTC 664
[8] *Case F138* (1984) 6 NZTC 60,237 at 60,244
[9] *Case Q55* (1998) 15 NZTC 5,313
[10] *Case H97*(supra)
[11] At 5,318
[12] At 5,320

> retain that connection on a durable basis, with that locality. I do not think that a durable connection with a locality alone could create "a permanent place of abode" where a dwelling is not owned or tenanted or otherwise available such as the house of a parent, or relative, or friend. I consider that the phrase "has a permanent place of abode" requires, inter alia, the availability of a place in which to dwell but that the existence of a home or dwelling does not necessarily create a permanent place of abode. The latter concept also requires some durability of connection with a locality as well as the availability of the place in which to sleep. There must be many people who have no permanent place of abode. Some of these people may have a number of residences.

He went on to observe that the paramount factor in assessing residency is the strength of a person's ties with New Zealand. He said[13]:

> I think that the strength of a person's ties with New Zealand is the paramount factor in assessing residency but those ties must include the availability on a permanent basis (continuing indefinitely) of a place in which to dwell and sleep if that person is to have a permanent place of abode somewhere in New Zealand. The enduring availability of a dwelling is a fundamental criterion to having a permanent place of abode, but it is not decisive on its own.

SUBMISSIONS

[35] Both counsel made extensive submissions which are summarised as follows.

(a) Place of Abode

[36] The Commissioner submits that the disputant had an available dwelling in New Zealand being the Esplanade property.[14] The disputant contends that the Esplanade property is a business asset not a home. The disputant never lived at this property. The facts therefore differ from those in *Case Q55, Case F138* [15] and *Case J 98.*[16] In each of those cases, the disputants had homes where they resided and which were filled with their furniture. They went overseas for short periods tenanting their homes. Here the disputant did not have any home in New Zealand at the time of his departure and left to pursue his career in the security industry overseas.

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[13] At supra
[14] It is not submitted that any of the other properties owned by the disputant was an available dwelling
[15] *Case F138* (1984) 6 NZTC 60,237
[16] *Case J 98* (1987) 9 NZTC 1,555

[37] The Esplanade property has been tenanted since 1998. Mr Colman for the disputant submits that this asset is locked into a complex ownership structure which it is not possible to resolve because of cross guarantees on the various properties. Furthermore there is no record as to the beneficial ownership arrangements which were merely the subject of an understanding between the parties. Mr Colman says that in terms of the Residential Tenancies Act 1986 the disputant is not in a position to exercise the powers of a landlord in an unrestricted manner as he is not the legal owner of the property. He submits that AB's consent would be needed if any notice was to be given under the Residential Tenancies Act 1986 and AB was unlikely to provide any such consent until all her interlocking property holdings and issues were resolved to her satisfaction. In her evidence, AB stated that she would not consent to the disputant trying to evict the tenants because an LAQC cannot rent property to an owner/occupier. In these circumstances Mr Colman says that the disputant does not have immediate and enforceable rights in respect of the Esplanade property which cannot be interfered with or defeated by others.

[38] Further, Mr Coleman submits that there was no evidence that the disputant intended to return and live in the Esplanade property. In other cases where the Commissioner has contested residence, there has been evidence of an existing abode to which the taxpayer intended to return.[17]

[39] Mr Lemmon for the Commissioner submits that it is acknowledged by the disputant and AB that the Esplanade property is beneficially owned by the disputant although since August 2005 it has been held in the name of Company X. The disputant pays the mortgage and expenses and contributes towards servicing the interest on the loans secured over the property.

[40] The Esplanade property has been rented out on a periodic tenancy rather than on a fixed term basis and the landlord in the relevant tax years was either the disputant or Company X. Mr Lemmon submits that this situation is analogous to that in *Case Q55*. While the taxpayer in that case had leased the residence he had lived in and would return to, the taxpayer also had other investment properties from which he received rental income and which the Authority thought would qualify as

possible places of abode if they had been required. Mr Lemmon says that the same situation is present in this case and that the Esplanade property similarly qualifies as a possible place of abode to which the disputant could have returned.

[41] Mr Lemmon contends to the extent that Company X legally owned the Esplanade property, that the disputant was in control of it. The transfer of the property into Company X was for tax purposes and did not change the understanding of the disputant and AB that it was the disputant's property. This situation did not alter following the execution of the Separation Agreement. That Agreement while dealing with other properties owned or controlled by the disputant and AB, did not address the legal or beneficial ownership of the Esplanade property and refers to the parties' interests in Company X remaining the same.

[42] Mr Lemmon submits that the location of the Esplanade property is also close to the disputant's other connections to New Zealand. The Commissioner therefore contends that this address would have been available to the disputant as a place at which he could have based himself upon his return to New Zealand if required. Mr Lemmon says that even though it might be suggested that AB may have prevented the disputant from accessing the property, such a suggestion runs contrary to the clear and repeated evidence that the property was beneficially owned by the disputant.

(b) Intention to be away permanently

[43] Mr Colman submits that when the disputant left New Zealand in July 2003 it was his intention to leave the country permanently. It is necessary to look not only at the disputant's intention but what actually occurred.[18] In this case the disputant has not lived in New Zealand since 2003 (apart from holidays) and has worked predominately in Iraq after that time. The disputant was not simply away from New Zealand for a year on sabbatical as was the position in *Case F138* or 18 months as in *Case F139* but has been away now for 10 years.

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[17] *Case H97, Case Q55, Case F138* and *Case J98*
[18] *Case F139* (1984) 6 NZTC 60,245

(c) Employment

[44] Mr Colman submits that the status of the disputant's employment is also relevant. In *Case Q55* and *Case F138* the taxpayers continued to be employed by a New Zealand employer while they were abroad. This was held to be a strong factor in support of the proposition that those taxpayers had a permanent place of abode in New Zealand.

[45] In the present case the disputant left New Zealand in 2003 and was employed by overseas entities. His employment involved carrying out security work in hot spots around the world (Papua New Guinea and Iraq) which could not be undertaken in New Zealand.

(d) Other ties with New Zealand

(i) Time spent in the country

[46] Mr Lemmon submits that even though the disputant worked outside New Zealand he was in the country for more than an incidental time. He spent about 42 days a year in New Zealand in each of the tax years in question.

(ii) Family relationships

[47] Mr Lemmon contends that the disputant continued to have a strong ongoing relationship with AB. through the relevant tax years. As well as being the mother of four of his children, AB is the disputant's business partner and also managed all the disputant's investments in New Zealand held in his own name and also through Company X. AB held Powers of Attorney and was the nominated emergency contact person for the purposes of the disputant's employment in Iraq. She was also executor of his Will. Until March 2011 AB had access to the disputant' salary paid into his Fort Worth bank account. As well, the disputant used her home address as his contact address in New Zealand.

[48] Mr Lemmon further contends that the disputant continued to financially support his four children to AB and maintained somewhat regular contact. He also provided financial support for his fifth child whom he saw on visits to this country.

[49] On the other hand Mr Colman makes the submission that the disputant's family and social ties were very limited. The time spent with his children on his visits to New Zealand was minimal. While the disputant continued to provide financial support for his former family Mr Colman submits that the provision of such support does not mean that the disputant had a permanent place of abode in New Zealand in the relevant years. He says that the disputant's position is similar to that of the taxpayer in *Case U17*.[19] There the taxpayer separated from his wife and became estranged from his children. Following that separation he went to live in Singapore. While living in Singapore the taxpayer purchased a dairy farm in New Zealand in order to provide for his family and also as an asset against which he could finance his Singapore business. The taxpayer travelled to New Zealand frequently to attend to matters relating to the dairy farm and to the business of a company in which he remained a director. On these visits he stayed with his mother or in a house on the farm. The taxpayer was away from New Zealand for five years between 1990 and 1995. The Taxation Review Authority found that the taxpayer had abandoned his permanent place of abode in New Zealand between 1990 and 1994.

[50] Mr Colman submits that the facts pertaining to the disputant's situation are stronger in support of the disputant's position that he did not have a permanent place of abode in New Zealand. In particular, the disputant:

(i) separated from his wife and has not lived in the marital home since August 1994;

(ii) is estranged from his children;

(iii) went to live overseas and has been working in Iraq ever since which is for a period of over 10 years;

(iv) has a 1% shareholding in Company X where he is nominally a director but has no involvement in the running of the company which has been undertaken by AB;

[19] (1999) 19 NZTC 9,174

(v) owns two blocks of bare land and two blocks of Maori land which he inherited as well as the beneficial ownership in 1½ rental properties held in Company X;

(vi) visits his mother and small daughter intermittently when here.

(iii) Investments in New Zealand

[51] Mr Colman further contends that merely owning investments in New Zealand also does not give a person a permanent place of abode in this country. In support of that contention he submits firstly, that the policy objective of the rules in s OE (1), (2) and (3) is to provide tests for residence in New Zealand based on length of time spent in this country. These would not be needed if mere ownership of New Zealand assets made a person a New Zealand tax resident.

[52] Secondly, in *Case U17* the taxpayer owned a dairy farm in New Zealand which is a substantial investment but nevertheless he was held not to be a New Zealand tax resident. In that case the taxpayer's economic wellbeing was not exclusively wrapped up with New Zealand. In contrast in *Case Q55* the taxpayer derived dividends from around eleven New Zealand companies. He continued to receive his salary from his New Zealand employer into his New Zealand bank account and received rental income from five New Zealand rental properties. These holdings were also not determinative of his status.

[53] In the present case, Mr Coleman submits that the bare land is not deriving any rental. The 1½ rental properties which the disputant owns beneficially through Company X produce rental income which largely goes to debt servicing. The disputant's one share shareholding in Company X is not material. Mr Colman contends that the disputant does not have extensive economic holdings in New Zealand and it cannot be said that his economic wellbeing is exclusively tied up with New Zealand. On the contrary, his overseas income is the source of his economic wellbeing and has been used to support his investments in this country.

[54] Mr Lemmon submits that while the disputant has earned most of his income overseas, he has invested his money in property in New Zealand. This has included the Esplanade property, the rental property partnership with AB, the two blocks of

bare land and Company X. As well, the disputant has interests in two blocks of Maori land. It is accepted that this land cannot be realised.

(iv) Other property

[55] Evidence was given that the disputant disposed of his vehicles (except the bike) in the period after he left New Zealand. The disputant did not have any New Zealand credit card. The New Zealand bank accounts were for mortgage payments. As well, the disputant had a pension and life insurance policy in New Zealand. In *Case F139* Judge Barber considered the fact that the disputant had sold his New Zealand car pointed to him not being a New Zealand tax resident. Furthermore, in the same case, Judge Barber considered that having New Zealand bank accounts and credit cards were neutral factors.

(v) New Zealand tax involvement

[56] Mr Lemmon further contends that the disputant also had a New Zealand tax involvement by virtue of his participation in the financial and tax affairs of AB during the relevant tax years. Company X was set up to allow AB to offset rental losses against her personal income. As a shareholder in the LAQC, the disputant was required to make an LAQC election. This was done by the disputant through AB exercising her power of attorney. As well, the disputant returned income tax as a resident for the income tax years ending 31 March 2004 and 2005.

(v) Connections outside New Zealand

[57] The Commissioner submits that it is also relevant that the disputant had no strong connections outside New Zealand during the tax years in question. The disputant was principally employed in Iraq during the relevant period. The disputant's contracts were for 13 month periods. Accommodation and food was provided and he had few personal possessions in Iraq. He took leave breaks outside Iraq. The Commissioner submits that this is in contrast to *Case U17* in which the taxpayer established a domestic life for himself in Singapore.

[58] In reply the disputant says that the security situation in Iraq meant that apart from performing his security duties, there was little opportunity for the disputant to leave the compound where he was living. In these circumstances the disputant submits that little weight can be placed on this factor.

DISCUSSION

[59] The tax years in question are 2004 to 2007. In determining whether the disputant had a permanent place of abode in New Zealand in the relevant years it is necessary to take into account the totality of the circumstances.

[60] The first issue for consideration is whether the disputant had an available dwelling in New Zealand in the relevant tax years. The facts in this case differ from many of the other residency cases. The disputant was a soldier and had moved around. He did not have a family home containing his own furniture and personal belongings at the time he left the country in July 2003.

[61] He did however own a house being the Esplanade property. This property was rented by the disputant on a periodic tenancy basis from 1998. In my view the fact that it was used as an investment property in this period is not a decisive factor. In *Case Q55* Judge Barber stated:[20]

> [The objector] derived rental income from about five rental properties in New Zealand. I accept that there would have been practical difficulties in he and his wife taking out residence in any of those properties, but they support an enduring relationship with New Zealand during the sabbatical period. At least one of the investment properties could be regarded as a potential place of abode for the objector and his wife had they needed it. They could have dwelt or lived there.

[62] In the present case, the Esplanade property was legally owned by the disputant in the 2004 and 2005 tax years and he could have served the requisite notice under the Residential Tenancies Act 1986 if at any time he had wished to return to New Zealand and to live in the property.

[63] During the 2006 tax year (August 2005) the Esplanade property was transferred to Company X in which the disputant was a director and held one share. I

do not accept that as a consequence of this transfer, the Esplanade property ceased to be an available dwelling. In her evidence AB stated that she would not have allowed the disputant to live in the Esplanade property and gave as her reason that this would not have been permissible as Company X was an LAQC. While there was no written agreement, both the disputant and AB were clear in their evidence that the disputant was the beneficial owner of the Esplanade property. Company X held the Esplanade property in effect on a constructive trust in favour of the disputant. It was apparent from the evidence that AB and the disputant maintained a close business relationship built on mutual trust. The transfer of the Esplanade property to Company X was done principally to assist AB for tax purposes. I consider that it would have been unlikely against this background that AB would have refused to cooperate with the disputant to obtain possession of the Esplanade property if he had required it even if there had been some tax implications as a result. The alternative would have been for the disputant to take legal action to obtain legal title to this property. In these circumstances I am of the view that the Esplanade property was an available dwelling during all the relevant tax years.

[64] Importantly this property was situated in a locality where the disputant had continuing family and other economic ties. The provincial town was where his former wife and children lived. As well he owned rental properties in partnership with AB in the area and in the 2006 year he purchased a bare block of land also in the area.

[65] In this case the disputant's employment involved carrying out security work in hot spots around the world. His employment had no association with New Zealand. It was work that could not be carried on in New Zealand and would inevitably take him overseas for long periods. In the 12 month period from July 2003 the disputant was employed on a 12 month contract in Papua New Guinea. There was no evidence of any right of renewal of that contract. In Iraq he was employed on 13 month contracts. While there was no certainty of employment the contract was rolled over once during the relevant tax period and was rolled over regularly after that.

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[20] Case Q55 at 5,319

[66] No contemporaneous documentation was produced as to the disputant's intention to leave New Zealand permanently in July 2003. Mr Coleman referred to a letter written by an insurance broker to the disputant dated 31 March 2006 following a request for forms to be able to withdraw the funds "due to Permanent Emigration." This was written by a third party almost three years after the disputant left and I am not prepared to put any weight on it. The disputant however continued to work in Iraq until 2012 and is now working in Australia. The length of time which he has spent out of New Zealand favours the disputant's position that he did intend to leave New Zealand permanently in 2003 but it is not determinative.

[67] This is not a case where the disputant left New Zealand and was continuously absent for a number of years. In the 3 years and 9 months between July 2004 and 31 March 2007 the disputant returned for visits every 5 - 6 months. He spent 42 days on average in New Zealand in this period. These visits were principally to see family.

[68] While the disputant's relationship with his children may have broken down in recent years I am satisfied that the disputant maintained an ongoing relationship with them in the tax years in question. The disputant endeavoured to speak to the children every Sunday while he was in Iraq. When in New Zealand he spent 2 – 5 days with his ex- wife and children (his visits were on average about 2 weeks). He also had holidays with them in other countries.

[69] The disputant continued to pay child support and other expenses for the children in this period. Mr Colman submits that meeting a person's moral obligation by the payment of child support is not sufficient to establish a permanent place of abode and refers to the decision of Judge Willy in *Case U17*. In that case however the taxpayer had been estranged from his children which I am satisfied is not the situation in the relevant tax years here.

[70] As well as his relationship with his children the disputant maintained a close relationship with AB which continued after he left New Zealand. AB was in effect the disputant's financial advisor and business partner. She held powers of attorney

and managed his affairs in New Zealand. Her address was his contact address in this country.

[71] The disputant's pay from his Iraqi employment in the relevant years went into his Fort Worth bank account. AB operated a debit card on this account and apart from the disputant's holiday and miscellaneous expenses in Iraq, on the evidence all the disputant's income continued to be spent in New Zealand (with his knowledge and approval) either on child support and expenses for the children or in relation to his property investments.

[72] I consider that in this case the disputant's continuing relationship with his children (including his financial support) and with AB is a significant factor in favour of finding that the disputant's permanent place of abode remained in New Zealand in the relevant tax years.

[73] In *Case U17* the taxpayer also kept real and personal assets in New Zealand. Judge Willy considered that this was fully explained by his responsible desire to provide for his family in New Zealand and as an asset base against which he could finance his business in Singapore. He observed that the taxpayer might have chosen any country to locate such assets but New Zealand was the obvious place because his family lived here, he was a New Zealander and he understood the business environment. In the present case I consider the disputant's property investments were more closely linked to New Zealand because of his ongoing business relationship with AB to whom he had provided support by agreeing to be on the title to various properties and permitted the shareholding in Company X to be structured so as to enable AB to claim the tax losses. He had investments in the Esplanade property and the rental property partnership before he left the country. He continued to invest in New Zealand and in the 2006 tax year he purchased two bare blocks of land (on AB's advice) and became a shareholder in Company X.

[74] In *Case U17* the Authority put weight on the efforts that the taxpayer made to establish himself in Singapore for example he opened bank accounts, leased a car, employed household staff, had a local doctor and learned to speak Malay. After two years the taxpayer applied for and was granted permanent residence. In the present

case the disputant did not establish any roots in Iraq. I accept the disputant's submission that this is hardly surprising when because of security issues, his leisure time was restricted to the compound where he was living. In view of the nature of the disputant's employment I do not place any particular weight on this factor.

[75] The disputant continued to maintain bank accounts in New Zealand for mortgage payments but no other bank accounts or credit card. He had a superannuation fund which he could not access until he was 60 and a New Zealand life insurance policy. Again I see these as neutral factors. Likewise I do not place any weight on the disputant's New Zealand tax involvement which I see as largely as an adjunct to his business interests with AB.

[76] The disputant transferred the ownership in his vehicles to AB in the following two years after he left New Zealand apart from the motor bike now abandoned on AB's property. This situation differs somewhat from that of a person who sells his motor vehicle to a third party at the time of his departure. In this case I do not consider that the disputant's actions support the view that he had formed an intention to leave this country permanently when he departed in July 2003 and again I do not place any particular weight on this factor.

[77] While there are some factors supporting the disputant's position I consider looking at the circumstances overall, that the disputant continued to have a strong and enduring relationship with New Zealand in the relevant tax years. He continued to have an available dwelling to return to and maintained close family and financial ties to this country. Taking into account all the matters discussed above I am of the view that the disputant had a permanent place of abode in New Zealand in the tax years ending 31 March 2004, 31 March 2005, 31 March 2006 and 31 March 2007.

SHORTFALL PENALTY FOR UNACCEPTABLE TAX POSITION

Legal Issues

[78] The Commissioner submits that a shortfall penalty for taking an unacceptable tax position applies. Section 141B of the TAA provides that a taxpayer takes an

unacceptable tax position if "viewed objectively, the tax position fails to meet the standard of being about as likely as not to be correct".

[79] A taxpayer is liable to pay a shortfall penalty if that taxpayer takes an unacceptable tax position and the tax shortfall arising from the taxpayer's position is more than both (a) $20,000 and (b) the lesser of $250,000 and 1% of the taxpayer's total tax figure for the relevant return period. A tax shortfall is the difference between the position taken by the taxpayer and the correct position. In the present case, as I found that the disputant is liable to pay tax, there is a tax shortfall. While the figures have still to be determined it was not in issue that they will meet the monetary threshold set out above.

[80] The phrase "about as likely as not to be correct" was considered in *Ben Nevis Forestry Ventures Limited v Commissioner of Inland Revenue*[21]. Tipping, McGrath and Gault JJ stated:

> **[184]** On its terms this standard does not require that the appellants' tax position had a 50 per cent prospect of success but, subject to that qualification, the merits of the arguments supporting the taxpayer's interpretation must be substantial. The stipulation of an objective test means that the taxpayer's belief that the position taken was correct, or not unacceptable, is irrelevant.
>
> **[185]** There is a helpful observation of Hill J concerning the statutory standard made in the context of a similar provision in Australian legislation:
>
> > " The word 'about' indicates the need for balancing the two arguments, with the consequence that there must be room for it to be argued which of the two positions is correct so that on balance the taxpayer's argument can objectively be said to be one that while wrong could be argued on rational grounds to be right."
>
> Whether a taxpayer's interpretation meets the standard in any case accordingly comes down to a judgment of the weight of the arguments that support the taxpayer's position in the application of the law to the relevant facts. The Act requires that the application of all tax laws, including the general anti-avoidance provision, be taken into account in making this judgment.[22] As well, discussions of the courts and Taxation Review Authority on the interpretation of relevant tax laws must be considered.[23]

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[21] (2009) 24 NZTC 23,188 (SC)
[22] Section 141B(7)(a)TAA
[23] Section 141B(7)(b) TAA

Submissions

[81] Mr Colman submits that the disputant's case is either (a) considerably more favourable to a finding of non-residence than similar cases where residence was found; or (b) equal to or stronger than the facts in cases where non-residency was confirmed.

[82] Mr Colman further submits that it requires judgment and discernment to get residency status correct. Facts need to be evaluated and their relative weight assessed. Mr Coleman submits that the plethora of cases on the subject belies the fact that the line is not clearly defined and the facts are critical to the final result. Moreover, in public statements issued by the Commissioner[24] it says that the Department accepted that an absence of 3 years would generally be enough for a person to be a non-resident.

[83] Finally, Mr Coleman submits that it is also relevant that while the test is objective, it is judged from the perspective of the objective reasonable taxpayer not from the perspective of a hypothetical sophisticated tax professional or large corporate. Mr Coleman submits that while the disputant would pass even that higher test, the Commissioner's argument wrongly assumes that the disputant is a sophisticated tax professional rather than a soldier.

[84] The Commissioner on the other hand contends that the evidence that there was a strong and enduring relationship with New Zealand and therefore a permanent place of abode was overwhelming. Any argument that there was no liability to pay tax is not "about as likely as not to be correct" and cannot succeed.

Discussion

[85] Each case is determined on its own facts and involves an objective enquiry. For the reasons set out above I have found that the disputant had a permanent place of abode in New Zealand in the tax years in question. I accept the disputant's submission that it requires judgment and discernment to get residency status correct.

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[24] TIB role 11 number 10 (November 1999) and PIB 180 (Example 3 of that document).These were not produced at the hearing

However in my view the merits supporting the disputant's arguments (discussed above) were not substantial particularly when the circumstances are considered in their totality.

[86] Mr Colman also places reliance on the Commissioner's public statements that an absence of 3 years would generally be enough for a person to be a non-resident. There was no evidence that the disputant knew of these statements and relied upon them. In the tax years in question the disputant was away for a total of 3 years and 9 months.

[87] In all the circumstances I find that the tax position taken by the disputant fails to meet the standard of being "about as likely as not to be correct" and the disputant is liable to pay a shortfall penalty for taking an unacceptable tax position in each of the relevant tax years. Those penalties are reduced by 50% for previous behaviour under s 141FB of the TAA.

DECISION

[88] I find that the disputant had a permanent place of abode in New Zealand in the 2004, 2005, 2006 and 2007 tax years and was a New Zealand tax resident in those years pursuant to s OE1(1) of the ITA 1994 and ITA 2004.

[89] I further find that the disputant is liable for a shortfall penalty in each of the tax years in question for taking an unacceptable tax position under s 141B of the TAA in an amount still to be fixed.

[90] The proceeding is to be set down for a further hearing to address quanta if the parties remain unable to agree the same.

Judge AA Sinclair
Taxation Review Authority