

31 October 2018

Public Consultation
Office of the Chief Tax Counsel
Inland Revenue
PO Box 2198
Wellington

Via email: PublicConsultation@ird.govt.nz

Dear Sir / Madam,

PUB00314: Income tax — bright-line test — farmland and main home exclusions — sale of lifestyle blocks

Thank you for the opportunity to comment on the draft item and provide feedback.

In summary, our submissions are as follows:

- Overall we believe the draft statement is clear and will be helpful for taxpayers;
- It should apply to property held in a trust, or explain why trusts are not included;
- The explanation of “in connection with or for the benefit of the dwelling” is helpful and clear; and
- The QWBA should include additional examples.

Background

The “bright-line test” applies to residential land sold within a certain period of time after purchase. Farmland is not residential land. If the land is residential, the sale will not be taxable if the “main home” exclusion is satisfied.

The draft QWBA clearly explains the ordering of the tests. It also includes a flow chart on page 3 which we found very clear and logical.

Absent the exceptions to the main home exclusion being a factor it would seem reasonable to expect that the “main home” exclusion would typically be available to the seller of a lifestyle block if it was not capable of being categorised as “farmland” due to the area of land involved and/or the use to which it is put.

Thus, we would expect the QWBA to explain when the exclusions will apply and also highlight situations where the lifestyle block may not satisfy one or other of the exclusions, or more rarely where both exclusions may not be available.

Scope of the QWBA

Paragraph 4 states that the QWBA will not apply to property held in a trust. This raises an issue as to whether the exclusions will apply differently if the property is held in a trust.

We would have thought that the test for the “main home” exclusion would apply equally to lifestyle blocks held in trust. The same principles should apply subject to the ‘principal settlor’ rules under section CB 16A(1)(b). If the property is the “main home” of one of the beneficiaries, the exclusion will prima facie apply and it will then be necessary to see whether the other tests explained in the QWBA are met.

We believe the QWBA should confirm that the same tests will apply to lifestyle blocks held in trust that prima facie satisfy the “main home” exclusion, or it should explain why trusts have not been included.

“In connection with or for the benefit of the dwelling”

The draft QWBA clearly explains when residential land is used “in connection with or for the benefit of the dwelling”. In the case of a lifestyle block, this may be land beyond the basic dwelling and curtilage. The explanation is helpful and we agree with the reasoning in paragraphs 30 and 31.

When does a lifestyle block become “farmland”?

The bright-line test only applies to “residential land”. It does not apply to “farmland”. Once a component part of the lifestyle block meets the definition of “farmland” the totality of the lifestyle block should not be subject to the bright-line test. This is well explained by the flow chart on page 3 of the draft QWBA. In addition, paragraph 20 explains that once land is “farmland”, the whole area of land, including the farm house, will generally be regarded as “farmland”. Unlike the “main home” exclusion, there is no predominate land use requirement.

Example 3 (on page 9 of the draft) concludes that the property was not “farmland”. However, the “main home” exclusion was available because three of the five hectares were used for a dwelling.

The comment made in the example that the avocado plot “was not being worked in an agricultural business carried on by Tom and Jess...” could be misconstrued by readers as the reason why the property was not considered to be “farmland”. This would not accord with the definition of “farmland” and the comments made in paragraphs 7 – 8 of the QWBA (in particular the second limb). Presumably the land was not considered “farmland” because the particular area leased by the avocado leasing company was not sufficient in its own right to support a commercial venture. This should be clarified.

We would see benefit in a further example where the two hectares would qualify as “farmland”. There will be some agricultural businesses which due to the high value ascribed to the produce grown do not require a large amount of land to be economically viable.

If the two hectares were planted as a hydroponic garden with high end niche produce/herbs, and this was found to be capable of being carried on as an agricultural business, the whole of the lifestyle block should qualify as “farmland”.

“Main home” exclusion

We would like to see further variations on the examples provided to deal more comprehensively with the “main home” exclusion. In particular it would be useful for the draft QWBA to highlight the situations where the lifestyle block neither satisfies the “farmland” or “main home” exclusions.

To take again example 3 on page 9, what if three hectares were in avocados (and this was still viewed as not being sufficient to constitute a commercial activity) and two hectares used for the house, garden and horses?

In this situation if the three hectares are leased to the avocado leasing company, we would expect based on comments in the QWBA, that the sale would be taxable because the dwelling does not satisfy the 50% land area test. That is, the leasing of the land precludes it from being available for use as a dwelling (in the wider context) to the seller.

This can be contrasted with Tom and Jess working the avocado plot themselves as either a hobby farm/activity or simply leaving the trees untended. In this situation the “main home” exclusion should be available as the whole five hectares should count for the predominant use test. Based on paragraph 31 the land area planted in avocados will either represent land for hobby farming or an area to enhance the enjoyment or aesthetic value of the dwelling (both being considered land used for a dwelling).

The above variations show that the rules will produce some arbitrary results and we believe more examples would be helpful to illustrate this point.

We would be happy to discuss our submission with you. Please contact Jolayne Trim on Jolayne.trim@charteredaccountantsanz.com.

Yours sincerely



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