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Tax case: Diamond v Commissioner of Inland Revenue

The Taxpayer was not a New Zealand resident for tax purposes

Diamond v Commissioner of Inland Revenue **[2014] NZHC 1935**

Background

The Commissioner (''the CIR") assessed the taxpayer, for income tax under s OE 1(3) of the Income Tax Act 1994 and the Income Tax Act 2004 (Income Tax Act 2007, s YD 1) for the years ending 31 March 2004 to 31 March 2007 on the basis that the taxpayer was resident in New Zealand for tax purposes as he had a "permanent place of abode" in New Zealand.

The CIR accepted that in each tax year in question, the taxpayer was absent from New Zealand for a period or periods exceeding 325 days.

The Taxation Review Authority ("TRA") upheld the CIR's approach. The High Court overturned the TRA's decision and held that for tax purposes the taxpayer was not a New Zealand resident.

The issue

The principal issue before the High Court was whether the TRA's approach to the meaning of a "permanent place of abode in New Zealand" was correct.

Facts

The taxpayer was born in New Zealand in 1960 and is a New Zealand citizen. From 1987 until June 2003, the taxpayer served in the New Zealand Army. He left New Zealand at that time and worked in Papua New Guinea as a security consultant with AusAid. Between July and October 2004 the taxpayer holidayed and worked in Queensland. He then worked until 2012 as a security guard in Iraq employed by a United States Corporation, DynCorp. More recently the taxpayer has lived in Australia. The taxpayer, who the TRA assessed as a credible witness, said that in June 2003 his intention was leave New Zealand permanently, and he had no intention of returning.

The taxpayer married his wife in 1981. For many years they lived in army accommodation. They separated in August 1994. At that time Mrs Diamond moved to Ngaruawahia with their children. Despite being separated, the taxpayer and Mrs Diamond remained in reasonably close contact. Among other things Mrs Diamond had direct access to the taxpayer's United States bank account into which his Iraq income was paid. Their children also from time to time had access to that account. Mrs Diamond managed the taxpayer's financial affairs in New Zealand. She held an Enduring Power of Attorney in relation to his personal care and welfare. Mrs Diamond's home address in Ngaruawahia was the taxpayer's contact address in New Zealand for many purposes including passenger arrival and departure cards, pay slips from his employer in Iraq and other documentation.

In 2006 the taxpayer formed a relationship with a New Zealand woman he met at the Gallipoli commemorations that year. The relationship did not last, but a child was born. Mrs Diamond arranged for maintenance payments to be made for that child from the taxpayer's United States bank account.

During the tax years in issue the taxpayer visited New Zealand every five or six months. He stayed with Mrs Diamond for between two to five days to see his children. He would also visit his mother, and other family members. During those years nearly all of the taxpayer's income was spent in New Zealand, either to support his wife in providing for their children's living expenses or to discharge mortgage obligations on the various properties he owned at that time.

Mr and Mrs Diamond's marriage was dissolved and relationship property matters were addressed in March 2009. At the time, and reflecting an ongoing relationship, the taxpayer made a will appointing his former wife as his sole executor and trustee.

It was the CIR's contention that the taxpayer's permanent place of abode in New Zealand was at 24 Waikato Esplanade, Ngaruawahia. He came to own that property in 1996 because when Mrs Diamond first moved to Ngaruawahia the house she first purchased was too small. She sold it and purchased the Waikato Esplanade property putting both her own name and the taxpayer's name on the title because the bank would not lend to her alone. Instead of paying child support, the taxpayer paid half the mortgage. Mrs Diamond lived at that address. The taxpayer did not. In 1998 Mrs Diamond moved house. The taxpayer had at that time cashed some army superannuation. Mrs Diamond contributed her share of that superannuation to purchase her new property and the taxpayer bought out her share in the Waikato Esplanade property. The property was rented out and held by the taxpayer as an investment property.

The taxpayer also owns other real property in New Zealand - two blocks of inherited communally owned Māori land, two blocks of bare land and a half share of a property in Raglan jointly with Mrs Diamond. In 2000 Mrs Diamond formed a partnership with the taxpayer to own rental properties. In 2005 Mrs Diamond incorporated a company to own the Waikato Esplanade property and another property. It was always understood that the taxpayer was the beneficial owner of the Waikato Esplanade property and half the other property.

The TRA's decision

Although noting there were some factors supporting the taxpayer's position, the TRA determined that the taxpayer had a permanent place of abode in New Zealand. Looking at the circumstances overall, the taxpayer had a strong and enduring relationship with New Zealand in the tax years in issue. He had an available dwelling to return to and maintained close family and financial ties to this country. Of particular significance was the taxpayer's ongoing relationship with his children, including his financial support of them and his ongoing relationship with Mrs Diamond. Other factors were that the taxpayer's employment contracts necessarily involved his absence from New Zealand, while there was no certainty of employment his contracts were in fact rolled over from year to year; there was no contemporaneous documentation supporting the taxpayer's intention to leave New Zealand permanently in 2003. The length of time he had actually spent out of New Zealand supported his intending to leave permanently but that was not determinative; and he had not been continuously out of New Zealand having returned from time to time, continued to pay child support and maintain a New Zealand relationship with Mrs Diamond.

The TRA in coming to its decision relied heavily on Judge Barber's reasoning in Case *Q55* (1993) NZTC 5,313.

Q *55* concerned a university professor who was absent from New Zealand while on a sabbatical. The professor had a home in New Zealand which he lived in immediately before and immediately after his absence on sabbatical leave. While away he rented out his house for a fixed period. The professor's absence was always intended to be (and was) a temporary one. The professor argued that he was not a tax resident of New Zealand during the year he was out of the country because his home was not available to him during his absence. The TRA held that in the circumstances the professor's rented property remained for him, a permanent place of abode. The TRA concluded it was a matter of fact as to whether or not a taxpayer had a permanent place of abode in New Zealand. Factors the TRA considered to be relevant in order to determine the issue were the reasons for going overseas, whether the taxpayer had established a permanent place of abode out of New Zealand; arrangements made by the taxpayer concerning his home in New Zealand; financial ties with New Zealand; other ties with New Zealand; and length of time out of New Zealand.

The TRA held in all the circumstances of the case the taxpayer had his permanent place of abode at his home in New Zealand prior to the taxpayer taking his sabbatical. Their letting of that home during his absence overseas did not stop that home from being his permanent place of abode.

The TRA said that the words "has a permanent place of abode" does not require that a dwelling be always vacant and available for the taxpayer to live in it 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 retain that connection on a durable basis with that locality. The facts of this case supported the view that the taxpayer had a permanent place of abode in New Zealand from which he was temporarily absent. That permanent place of abode was not available to him at all times when he was overseas (as it was rented on a short term fixed tenancy). However, on the facts it remained his permanent place of abode and in particular that the taxpayer had lived there prior to his temporary departure overseas on his sabbatical and that he intended to and did return there immediately after that period of leave expired. Further, the taxpayer during his one year absence retained a wide range of connections with New Zealand.

The application of Q 55 to the facts in Diamond

Clifford J held that *Q 55* is not authority for the approach taken by the TRA in this case. His Honour noted that the TRA took a two-stage approach to the issue, firstly, whether or not there was a dwelling available to the taxpayer to live in New Zealand, and then assess, by reference to the taxpayer's connections to New Zealand whether or not that available dwelling was to be characterised as a permanent place of abode.

Clifford J's view is that *Q 55* is authority for the proposition that a person's permanent place of abode in New Zealand will not cease to have that character merely because whilst the person is outside New Zealand for a period greater than the statutory deeming period (183 days), that dwelling is rented out. The dwelling can maintain its character as the person's permanent place of abode, dependent on the particular factual circumstances notwithstanding that fact. His Honour noted that nowhere in *Q55* is it suggested that a permanent place of abode in New Zealand may be a house that the taxpayer has never lived in. Nor does it say that the application of the test involves some assessment of the likelihood of the taxpayer returning to New Zealand and taking up residence in that house.

Clifford J considered whether the Waikato Esplanade property was the taxpayer's permanent place of abode based on the correct interpretation of s OE 1 (1). The ordinary meaning of "to have a permanent place of abode in New Zealand" is "to have a home in New Zealand". In Clifford J's view the significance of an appropriate degree of permanence is emphasised by the meaning of the noun "abode" being itself that of an habitual residence, a house or home. The taxpayer had at no time lived at the Waikato Esplanade property and for so long as he owned that property himself he had rented it out to others. The property was not the taxpayer's dwelling, or a home in New Zealand.

Clifford J determined the purpose of the provision noting that s 241 of the ITA 1976 provided that " A person … shall be deemed to be resident in New Zealand … if his home is in New Zealand".

The word "home" was replaced by the "permanent place of abode" test in 1980. Clifford J found the observations in *Federal Commissioner of Taxation v Applegate* (1979) 27 ALR 114 (FCA) helpful. Fisher J said that the meaning of "permanent place of abode" is that it is the taxpayer's fixed and habitual place of abode. It is his home, but not his permanent home. It denotes a more enduring relationship with a particular place of abode than that of a person who is ordinarily resident there or who has there his usual place of abode. Material factors were the continuity of the taxpayer's presence, the duration of his presence and the durability of his association with the particular place.

The Waikato Esplanade property had never been the taxpayer's home, it was not intended by him to be his home; it was never lived in by him; and it was purely used for investment and such use had continued for nearly 20 years. The taxpayer did have other ongoing personal connections with New Zealand but in the absence of the property having the characteristic of a permanent place of abode those connections did not alter the Court's conclusion that the taxpayer was not for tax purposes a New Zealand resident.

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