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Inland Revenue Department
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Dear Sir/Madam,

## When a disposal of land will be part of a profit-making undertaking or scheme subject to income tax under s CB 3 (PUB00519)

Thank you for the opportunity to comment on the consultation on draft Interpretation Statement **When a disposal of land will be part of a profit-making undertaking or scheme subject to income tax under s CB 3** (draft IS) of the Income Tax Act 2007 (ITA 2007)

CPA Australia represents the diverse interests of more than 176,000 members, including over 3,300 members in New Zealand, working in over a 100 countries and regions supported by 19 offices around the world. We make this submission on behalf of our members and in the broader public interest.

**Executive summary**

CPA Australia welcomes the opportunity to comment on Inland Revenue's draft interpretation statement on when a disposal of land will be part of a profit-making undertaking or scheme under section CB 3. While the draft provides useful conceptual guidance, we are concerned that applying section CB 3 as a residual taxing provision may undermine the certainty intended by the specific land-taxing rules and their statutory exclusions. In particular, greater clarity is needed on the boundary between mere realisation and a profit-making undertaking or scheme, the interaction with the bright-line test, and the evidentiary requirements for identifying when a scheme commences. We recommend that the finalised interpretation statement includes clear realistic examples, recognise a strong presumption against applying section CB 3 where a specific statutory exclusion is satisfied, and provide practical guidance to ensure Inland Revenue does not apply section CB 3 as a default alternative where the specific land provisions do not apply.

**Key comments and recommendations**

We make the following comments for your consideration:

- Section CB 3 should not operate as a residual or default taxing provision where a land transaction is not captured by the specific land-taxing rules. The finalised interpretation statement should make clear that section CB 3 requires a distinct factual and legal basis.
- The guidance should more effectively reflect the certainty intended by the specific land provisions and their statutory exclusions, particularly for long-held residential land, business premises and farmland.
- Inland Revenue should clarify the interaction between section CB 3 and the bright-line test under section CB 6A, including how the provisions apply where a bright-line exclusion is available.
- The finalised interpretation statement should provide more practical commentary on the distinction between mere realisation of a capital asset and a profit-making undertaking or scheme, supported by realistic taxable and non-taxable examples.
- Realistic examples should confirm that common realisation activities, such as obtaining consents, rezoning applications, basic land division and minor site preparation, do not of themselves amount to a section CB 3 scheme.

- The guidance should affirm that profit or an expectation of profit is not, in itself, sufficient to establish a profit-making undertaking or scheme.
- Inland Revenue should provide clear evidentiary guidance on when a scheme commences, including how taxpayers can support the commencement date for section DB 26 ITA 2007 market value deduction purposes.
- Section CB 3 should not be advanced routinely as an alternative assessment without clearly identifying the alleged scheme, its commencement date, its subject matter and the evidence supporting a dominant profit-making purpose.
- Consideration should be given to a targeted legislative amendment or priority rule to clarify the relationship between section CB 3 and the specific land-taxing provisions.

Please refer to the Appendix for our detailed discussions. If you have any queries about this submission, please contact me on jenny.wong@cpaaustralia.com.au or Bill Leung, Tax Technical Advisor on bill.leung@cpaaustralia.com.au.

Yours sincerely,

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**Acknowledgements**

CPA Australia would like to acknowledge the following Tax Committee members for their input and guidance in shaping this submission:

- Mr Angus Ogilvie FCPA (Aust.), Chair of Tax Committee – New Zealand
- Mr Peter Loerscher, CPA (Aust.), Tax Committee – New Zealand
- Mr Jeffrey Owens FCPA (Aust.), Tax Committee – New Zealand
- Mr Darshana Elwela – Tax Committee – New Zealand
- Mr Richard Ashby CPA (Aust.), Tax Committee – New Zealand
- Mr Jamil Eldar, CPA (Aust.), Tax Committee – New Zealand
- Professor Adrian Sawyer, FCPA (Aust.), Tax Committee – New Zealand

## Appendix

**Analysis of the Draft's Comprehensiveness**

**1. Code vs. non-code and section CB 3**

Parliament enacted sections CB 6 to CB 15 (and their predecessors) to establish clear, objective parameters for when amounts derived from disposals of land are treated as income under Part C. On of the fundamental question addressed by PUB00519 is whether Parliament intended sections CB 12 and CB 13 (the specific development and division rules) to replace the general application of section CB 3. Inland Revenue concludes they do not. The draft states that:

> *There is nothing to indicate ss CB 12 and CB 13 were intended to replace s CB 3 for land disposals.*

Therefore, income arises under section CB 3 where a taxpayer enters into a profit-making scheme involving land, even if the strict criteria of the specific land provisions are not met. Creating a dual-track assessment where land transactions must consider both the specific land provisions and a secondary s CB 3 analysis undermines statutory certainty and coherence.

**2. The "mere realisation" threshold and section CB 12**

To ensure section CB 3 does not treat all amounts derived from land disposals as income, the draft IS relies heavily on the "mere realisation" doctrine. A taxpayer can prepare a capital asset for sale at the best advantage without triggering section CB 3, provided they do not cross into a profit-making scheme.

The draft illustrates this boundary effectively using the "Jensen" scenario (Example 3). Jensen subdivides his residential section, demolishes the existing house, and builds two new dwellings, intending to sell one. Because Jensen held the land for more than 10 years before commencing the scheme, section CB 12 does not apply. However, the draft IS concludes that the gross proceeds are income under section CB 3 because:

> *Constructing a new dwelling to sell creates something new on the land, and completely changes its character. This goes beyond merely realising part of the taxpayer's land at best advantage.*

It is our members view that in itself, Example 3 will lead to further confusion within the taxpaying community, due to the Commissioner's prior publication of TDS 22/21 – where on similar facts (division of a residential section into two lots, two new dwellings constructed intending to sell one), Tax Counsel Office found for the taxpayer that the dominant purpose of the scheme was to provide a family home and not to make a profit. Furthermore, this was a scheme commenced within 10 years, but for which the taxpayer was able to rely on the residential exclusion contained in section CB 17(2) to exempt the disposal from taxation under section CB 12. As such, the reason IR considers the mere realisation exclusion does/does not apply in Examples 2 and 3 should be made clearer. We further submit that:

- The most basic activities essential for modern capital realisation at best advantage, such as obtaining resource consents, undertaking required civil infrastructure, or minor boundary adjustments, sit in an uncomfortable grey area.
- Requiring taxpayers to establish the exact point at which preliminary exploratory/feasibility work crosses into an assessable "undertaking" creates severe evidentiary uncertainty.
- The reason IR considers the mere realisation exclusion does / does not apply in Examples 2 and 3 should be made clearer.
- To what extent can the taxpayer "create something new on the land, and completely change its character" without being caught by section CB 3? Left as the present example is drafted, and based on recent "real world" experience with the Commissioner's representatives, members are concerned that adding anything "new" to the land during the realisation process will be interpreted by Inland Revenue investigators as meaning that they should be applying section CB 3 to the disposal.

**3. Protection of statutory exclusions**

The statutory design of subpart CB deliberately pairs broad land disposal provisions with specific exclusions to protect legitimate capital holdings (such as family homes, business premises, and agricultural land). Under the approach in PUB00519, a taxpayer who meets all statutory criteria for an exclusion in sections CB 6 to CB 15 remains vulnerable to being taxed under s CB 3. This defeats the clear policy objective of providing realistic for long-held capital assets.

A key concern for tax advisers is whether applying section CB 3 overrides the statutory exclusions granted to residential land (sections CB 16 and CB 17), business premises (sections CB 19 and CB 20), and farmland (section CB 21). The draft comprehensively navigates this by clarifying that these exclusions are designed to protect the disposal of land used mainly as a capital asset. Since section CB 3 only captures activities that go *beyond* the mere realisation of a capital asset, the exclusions are conceptually preserved.

**Areas for improvement and recommended changes**

While the conceptual framework appears logical in principle, the draft could benefit from specific changes to address practical gaps:

**1. Rebuttable presumption for statutory exclusions**
The final interpretation statement should explicitly clarify that where a transaction satisfies a specific statutory exclusion under sections CB 6 to CB 15 (e.g., section CB 16 for main homes or section CB 19 for business premises), there is a strong rebuttable presumption that section CB 3 does not apply. Section CB 3 should only be invoked in rare, exceptional cases involving a clearly severed, profit-making undertaking or scheme.

**2. Clear "realistic" examples for realisation activities**
The Commissioner should incorporate objective, s CB 6A bright-line examples within the finalised guidance demonstrating that common value-enhancement activities—such as obtaining consents, site rezoning applications, basic land divisions, and cosmetic site preparation—do **not** elevate a capital disposal into a s CB 3 scheme.

**3. Silence on the bright-line test (Section CB 6A)**
The most glaring omission in the exposure draft is its silence regarding the interaction between section CB 3 and the bright-line test in section CB 6A. Given the frequency with which residential property is captured by the bright-line test, practitioners need express guidance on overlap and priority. If a property is caught by both section CB 6A and section CB 3, or if a s CB6A(5) bright-line exclusion applies but the Commissioner seeks to apply section CB 3, the priority of these rules must be clear. The draft should be amended to explicitly address this overlap.

**4. Operational reality of s CB 3**
The concern is not confined to the wording of the legislation or the technical analysis in an interpretation statement. It also extends to how Inland Revenue applies those materials in practice. A principal concern, based on practical experience, is the increasing tendency for Inland Revenue officers to rely on section CB 3 as a residual taxing provision where a taxpayer is not otherwise captured by the specific land-taxing provisions. In particular, the treatment of section CB 3 as a residual provision risk reducing the practical significance of the detailed land provisions, their timing rules and their exclusions. The Jensen example illustrates that concern rather than resolving it.

For example, there is a risk that section CB 3 may be used as a catch-all provision where the Commissioner cannot establish liability under the specific land provisions. In practice, this could result in multiple taxing provisions being advanced in the alternative, requiring taxpayers to respond to each one.

One of our members have advised that in a recent matter that proceeded to the Tax Counsel Office, the Revenue team maintained that section CB 3 should apply if it is not assessable income under section CB 6, which was asserted on the basis that the property marketing material indicated the land could be subdivided (therefore acquired with a purpose or intent of disposal), or section CB 12, where it was asserted that the client could not rely on the residential exclusion because they had not lived in the newly constructed dwelling before sale. Our member's view is that position reflected a misinterpretation of the section CB 17 exclusion (which only requires the land was occupied mainly as residential land before it was divided). The Revenue team's underlying concern

appeared to be that the client had realised a profit on sale. The taxpayer was ultimately successful before the Tax Counsel Office on all grounds – not subject to section CB 3 because the dominant purpose of the scheme was found not to be profit. In another two separate examples, Commissioner's representatives telling our member that if absolute costs in a scheme of development or division exceed $50,000, then CB 12 automatically applies because the work is more than minor in accordance with the Commissioners views expressed in IS 20/08!

As such, guidance expressed as non-binding can become a de facto rule in audit practice. Unless PUB00519 contains clear examples of both taxable and non-taxable outcomes of section CB 3, there is a real risk that any case falling outside an expressly non-taxable example will be treated as taxable. Accordingly, the broader concern remains that unless the interpretation statement provides clear guidance on the "mere realisation" principle, supported by numerous practical examples of common scenarios in which section CB 3 should and should not apply, taxpayers and advisers will continue to encounter uncertainty.

In practice, Inland Revenue officers may seek to apply all potentially available taxing provisions, leaving taxpayers to discharge the onus of proof in relation to each provision. This issue is particularly acute because many taxpayers in these circumstances are not experienced land dealers, developers or builders, who would generally be subject to the specific business-related land taxing provisions. They are often ordinary homeowners who have held land for a significant period and, for example, may seek to downsize after their children have left home by subdividing and disposing of part of the property. In such cases, a profit may naturally arise (and in fact should be expected to, otherwise why incur the cost to do anything in the first place); however, that should not of itself justify the application of section CB 3. The central issue is whether profit was the dominant purpose, which may be difficult for non-specialist taxpayers to evidence, particularly where the issue arises retrospectively through a risk review and the taxpayer did not obtain tax advice before commencing the activity. In those circumstances, there may be limited contemporaneous evidence, beyond the taxpayer's own explanation, to demonstrate a non-profit-making dominant purpose.

There is a wider procedural concern as well. Practitioners continue to encounter short response deadlines imposed on taxpayers, lengthy delays in Inland Revenue's own responses, and investigation teams that appear reluctant to reconsider an initial position until the matter reaches to a high level. Our members advised the latter is becoming increasingly difficult with senior staff pushing contentious issues down to low level or anonymous staff. There are also occasional instances where communications with represented taxpayers can complicate the adviser relationship unnecessarily. These are not criticisms of Inland Revenue staff generally, but they are relevant to how a broad residual provision is likely to operate in practice.

PUB00519 raises similar concerns to IS 20/08, which addresses the "minor work" issue for section CB 12. While the guidance thresholds in IS 20/08, namely an absolute cost threshold of $50,000 or a relative value threshold of 5 per cent, were a significant improvement on the previous reliance on older case law, there is a risk that indicative thresholds may be applied too rigidly in practice. For example, where the cost marginally exceeds the stated threshold, the work may be treated as more than minor, with the result that the relevant taxing provision is considered to apply. A similar risk arises with PUB00519. Unless the final statement and examples clearly identify circumstances in which section CB 3 should not apply, taxpayers may be required to demonstrate that their circumstances fall outside a taxable profit-making scheme.

**4. Guidance on the "commencement" threshold**

The finalised statement must provide clear operational rules establishing that preliminary feasibility testing, market appraisals, and exploratory planning do not constitute the "commencement" of a profit-making scheme under s CB 3.

**5. Mechanics of deductions under section DB 26**

Where section CB 3 imposes a gross inclusion for the sale proceeds, section DB 26 provides the corresponding deduction mechanism. Section DB 26(3) sets out a "market value uplift", deeming the taxpayer to have:

> *(a) having disposed of the property to an unrelated third party immediately before the start of the undertaking or scheme; and (b) having reacquired the property immediately after the start of the undertaking or scheme at the market value of the property at the time.*

The gross proceeds are included under section CB 3, the market value of the property at the scheme's commencement is deducted under section DB 26, and the net difference is the taxable profit. While the draft mentions this mechanism, it lacks practical guidance on how taxpayers should evidence the exact commencement date of the scheme to secure the uplift. Without strict parameters on when the "first step" occurs, taxpayers face substantial valuation risk. The draft should include examples detailing the evidentiary requirements for this valuation.

**6. Legislative recommendation: order of priority rule**

We recommend that IRD signal to Policy and Regulatory Stewardship the need for a targeted legislative amendment, either inserting an explicit priority ordering rule in section CB 3 or codifying sections CB 6 to CB 15 as an exclusive framework for real property to permanently resolve the overlap.

**7. Further issues**

Two further matters also warrant consideration:

1. If Inland Revenue is seeking to minimise taxpayer uncertainty, consideration could be given to recommending a legislative amendment to clarify that section CB 3 does not apply to land transactions that are already addressed by a specific set of land-taxing provisions.
2. Consideration could also be given to refining the disputes process so that, once a matter reaches the conference stage, an appropriately experienced and independent officer within each office reviews the case afresh and provides separate commentary. This may assist in ensuring that positions taken in a notice of proposed adjustment or notice of response are reconsidered objectively before the matter progresses further. In practice, advisers may perceive that investigation teams are reluctant to alter their position once formal documents have been issued. A more independent review at conference stage could help reduce costs, improve procedural fairness and support earlier resolution of disputes.
3. Section CB 6 is inadequately addressed in the draft IS. It is only addressed in Example 5, there is no explanation in the guidance regarding how it fits with s CB 3. Sections CB 7 -11 should be similarly (albeit briefly) addressed for completeness.

**Conclusion**

Inland Revenue's exposure draft PUB00519 in principle establishes that the specific land sale rules are not an exclusive legislative code, confirming that section CB 3 operates as a residual taxing provision where a disposal constitutes a profit-making scheme rather than the mere realisation of a capital asset.

The draft IS provides conceptual guidance on this boundary, correctly asserting that the statutory exclusions for residential, business, and farming land are not undermined by section CB 3 because those exclusions fundamentally protect capital use.

PUB00519 introduces an unnecessary layer of risk and subjective testing to real estate transactions in New Zealand. We respectfully request that Inland Revenue refine the statement prior to finalisation by adopting clear realistic, respecting statutory exclusions, and providing definitive guidance on the limits of section CB 3.

However, the draft remains materially incomplete in its practical application, as it fails to explicitly address the interaction and priority between section CB 3 and the bright-line test, and lacks essential evidentiary parameters for taxpayers needing to prove the exact "first step" of a scheme to secure the market value deduction under section DB 26.

For that reason, the Inland Revenue should state expressly in the guidance that:

1. A profit or expectation of profit is not, by itself, sufficient to establish a profit-making undertaking or scheme. Perhaps with recognition by the Commissioner that most undertakings or schemes are likely to have profit outcomes simply due to the economic considerations by the taxpayer prior to commencement – the asset would be realised in its present state if incurring costs was not going to generate a better outcome.
2. The failure of a specific land provision does not create any presumption that section CB 3 applies and perhaps should create a presumption that it should not apply in a case where sections CB 12 and CB 13 have been considered, unless profit-making being the dominant purpose is very clear.

3. Section CB 3 should not be advanced routinely as an alternative without a distinct factual and legal basis.
4. The Commissioner should identify clearly the alleged undertaking or scheme, its commencement date, its subject matter and the evidence said to establish the required profit-making purpose.
5. The statement should include realistic examples where subdivision, construction or sale activity remains a mere realisation.

By addressing these shortcomings, the document would be enhanced as an extremely robust document with which to guide decision making and advice.

We welcome the opportunity to discuss these matters further or participate in working groups regarding the finalisation of this statement.