Receipts from Personal Exertion: 
Mere Gifts or Gross Income?

RANJANA GUPTA

A dissertation submitted to
Auckland University of Technology
in partial fulfilment of the requirements for the degree of
Master of Business (MBus)

2009

Faculty of Business and Law

Primary Supervisor: Professor Chris Ohms
CONTENTS

I. ATTESTATION ................................................................. ..........................I

II. ACKNOWLEDGMENTS .............................................................. II

III. ABSTRACT ........................................................................ III

PART ONE - OVERVIEW

1.0 INTRODUCTION ......................................................................... 1

1.1 ECONOMIC CONCEPT OF INCOME ........................................... 2

1.2 STATUTORY CONCEPT OF INCOME .......................................... 4

1.2.1 Overall Scheme of the Act ...................................................... 4

1.2.2 The Concept of Income ......................................................... 6

PART TWO - ANALYTICAL FRAMEWORK

2.0 THE NATURE OF RECEIPT .......................................................... 9

2.1 ORDINARY INCOME ................................................................ 10

2.1.1 Realisation ........................................................................... 12

2.1.2 Revenue in Nature ................................................................. 14

2.1.3 Capital Gains are Excluded .................................................. 19

2.1.4 Windfall Gains are Excluded ................................................ 20

2.2 SECTION CE 1 EMPLOYMENT INCOME ................................... 22

2.2.1 Employee and an Independent Contractor ................................ 24

2.2.2 History of s CE 1 .................................................................. 27

2.3 SECTION CB 1 BUSINESS INCOME .......................................... 30

PART THREE - A REVIEW AND ANALYSIS OF CASES

3.0 CATEGORIES OF GIFTS ............................................................. 38

3.1 GIFTS TO EMPLOYEES ............................................................ 39

3.1.1 Gifts in general ................................................................... 39

i Seymour v Reed ....................................................................... 39

II Hayes v FCT ........................................................................ 40

III Wright v Boyce ...................................................................... 42

IV Moore v Griffiths (Inspector of Taxes) .................................... 43

V Kelly v FCT ............................................................................ 45

VI Case V135 ............................................................................. 46

Theme .................................................................................... 47

3.1.2 Gifts made by employer to employee ................................... 48

I Laidler v Perry ........................................................................ 48

II Ball v Johnson ........................................................................ 49

Theme .................................................................................... 50

3.1.3 Contractual Receipts ............................................................. 50

I Blakiston v Cooper (Surveyor of Taxes) .................................... 50

II Mudd v Collins (HM Inspector of Taxes) ................................. 52

III Louisson v Commissioner of Taxes ....................................... 53

IV FCT v Dixon ........................................................................ 54

V Moorhouse v Dooland ............................................................... 56

VI Hochstrasser v Mayes (Inspector of Taxes) ............................ 58

VII Clayton (Inspector of Taxes) v Gothorp ................................ 59

VIII FCT v Harris ....................................................................... 60

IX Naismith v CIR .................................................................... 62

X FCT v Blake ........................................................................... 62

XI Reid v CIR ............................................................................. 63
PART 4 - THE CONCEPTUAL FRAMEWORK

4.0 WAYS TO ANALYSE GIFTS FROM PERSONAL EXERTION INCOME ........................................... 80
4.1 SECTION CE 1 EMPLOYMENT INCOME ..................................................................................... 80
4.2 SECTION CB 1 BUSINESS INCOME .......................................................................................... 85
4.3 SECTION CA 1 (2) SERVICES RENDERED .................................................................................. 87
4.4 SECTION CA 1 (2) PERIODICITY, RECURRENCE OR REGULARITY ............................................ 90
4.5 SECTION CA 1 (2) EXPECTATION OF REWARD ................................................................. 92
4.6 SECTION CA 1 (2) INTENTION OF THE DONOR AND DONEE .............................................. 94
4.7 TWO WAYS TO ANALYSE GIFTS FROM PERSONAL EXERTION INCOME ............................... 95

PART 5 - CONCLUSION ................................................................................................................. 99

APPENDIX .......................................................................................................................................... 104
REFERENCE ....................................................................................................................................... 106
Attestation of Authorship

I hereby declare that this submission is my own work and that, to the best of my knowledge and belief, it contains no material previously published or written by another person (except where explicitly defined in the acknowledgements), nor material which to a substantial extent has been submitted for the award of any other degree or diploma of a university or other institution of higher learning.

Ranjana Gupta
Acknowledgements

He has made His wonderful works to be remembered; 
the Lord is gracious and full of compassion. 
Psalm 111:4

There are many people I would like to thank for enabling me to complete my dissertation.

Firstly, I would like to express my deepest gratitude to Professor Chris Ohms for the scholarly support throughout this research process.

Secondly, I would like to thank Professor Ian Eagles, Dean of Law, Director, Centre for Commercial Law Research, Auckland University of Technology and Professor Louise Longdin, Director of Postgraduate Programmes in Law and Taxation, Auckland University of Technology for the support which has made my study a rewarding endeavour.

I also want to thank Professor John Prebble, Victoria University without whose encouragement, scholarly support and timely advise this dissertation would not have become a reality.

Special thanks are due to Gajan Satthianathan, Solicitor, Buddle Findlay, New Zealand Lawyers, for proof reading and prompt support throughout my research.

Finally, I would like to thank my family for their sacrifices, support and love.
ABSTRACT

This paper explores the gaps that exist with regard to the taxation of receipts from personal exertion. This research examines both the New Zealand legislation and leading cases in New Zealand and other jurisdictions in the area of receipts from personal exertion, to arrive at some conclusions about the circumstances in which those receipts will be found to be either gross income or simply a gift. To determine the legal criteria that identify gifts as personal exertion income within context of s CA 1(1) and s CA 1(2) of the Income Tax Act 2007, the paper sets out and analyse the following proposition:

   (1) Ordinary concepts (s CA 1(2)) includes employment income (s CE 1) and business income (s CB 1); or
   (2) Ordinary concepts (s CA 1(2)), employment income (s CE 1) and business income (s CB 1) are disparate tests.

The paper shows that sections CA 1(1) and CA 1(2) are not mutually exclusive and s CA 1(2) of the Act supplements specific provisions of the Act defining income.

In the absence of a clear statutory provision in the Income Tax Act 2007, the paper attempts to explain the underlying principles on which such receipts may be taxed within the broader context of the Income Tax Act 2007. The author hopes that this will serve as a guide for policymakers to take next step to ensure that unfairness caused by those deficiencies does not ultimately undermine the tax system.
Part 1
Overview

1. Introduction

This paper examines legislation and leading cases in New Zealand and other jurisdictions relating to the taxation of gifts as “income” in the particular context of receipts from personal exertion.¹ It looks at the scope, the strength and limitations of the law to arrive at a conclusion about the circumstances in which a receipt in return for personal exertion will be found to be either gross income or a mere gift.

The Income Tax Act 2007 (hereinafter referred to as ‘the Act’)² taxes net income (gross receipts less deductions). There is no statutory test of the overall concept of “income”, s CA 1(2) nor of personal exertion income specifically – it is a judicially created term of art. To examine taxation of personal exertion income, the paper considers the application of the key statutory provisions, ss CA 1 (2), CE 1 and s CB 1 of the Act. Gifts from personal exertion income may be analysed in two ways:

(3) Ordinary concepts (s CA 1(2)) includes employment income (s CE 1) and business income (s CB 1); or
(4) Ordinary concepts (s CA 1(2)), employment income (s CE 1) and business income (s CB 1) are disparate tests.

To analyse gifts from personal exertion income, the paper reviews leading cases under 3 categories –

a. Gifts to employees
b. Gifts to independent contactors
c. Gifts to businesses

Following on from this introduction, part 1 introduces and sets out the broad overview of the paper. Part 2 of the paper expands on analytical framework, specifically personal personal exertion income. Part 3 of the paper undertakes a review and analysis of the

¹ The earning activity is employment or the rendering of services (PEI). Hayes v FCT (1956) 96 CLR 47; Scott v FCT [1966] 117 CLR 514.
leading cases dealing with gifts from personal exertion income. Part 4 of the paper develops conceptual framework and part 5 concludes.

To examine the application of the key statutory provisions that is s CA 1 (2), s CE 1 and s CB 1 of the Act with regard to personal exertion income, the economic concept of income must be evaluated within the statutory framework of s CA 1(2), CE 1 and s CB 1.3

1.1 Economic concept of income
Economists cannot, it seems, agree on a single definition of income. Proposed definitions include (a) ideas of capital maintenance, income as a flow and the comprehensive income concept associated with the work of HC Simons.4 (b) the power to consume rather than the actual consumption5 (c) increase in the economic power of the recipient to control goods and services (d) an all encompassing concept recognising all gains as income regardless of the source or the form the gain takes.6

In economic terms the term “income” and “gain” are interchangeable terms, which correspond to increases in wealth.7 “Thus, the economist might define the income of a

3 The “income” envisaged by an economist may not be the same ‘income” that is liable to tax. The reason for this being that economists, who in the guise of the Treasury Department advise governments on income based concepts maintain fundamentally different beliefs as to the make-up of “income” than lawyers who have the task of interpreting legislation. The result therefore is that on occasion the “income” envisaged by economists may not be the same “income” that is liable to tax. Prebble has suggested that the concept of income is “in some senses an artificial construct, to the extent that it may almost be thought of as a fiction”, J Prebble, “Fictions of Income Tax”, (Paper presented at the 14th Annual Australasian Tax Teachers’ Association Conference, 2002), p 2, available at:


5 Robert Haig, “The Concept of Income – Economic and Legal Aspects”, in Haig, Robert M.(ed.), The Federal Income Tax, Columbia University Press, New York,1921 at p 7 Robert Haig states: “It [the economic income concept] has the effect of taxing the recipient of income when he receives the power to attain satisfactions rather than when he elects to exercise that power”.


period as the difference between what the taxpayer was worth at the beginning of the period and what he or she was worth at the end of the period, plus the value of his or her consumption during the period”. Simons saw the relationship between the time period and the income concept as being “fundamental”.

Every person’s accretion to wealth in any period falls within the tax base. Haig and Simons recognised that the receipt of gifts and windfall gains enhanced economic power and capacity of the recipient. Simons defined income as follows: “personal income may be defined as the algebraic sum of (1) market value of rights exercised in consumption and (2) the change in the value of the store of property rights between the beginning and end of the period in question. In other words, it is merely the result obtained by adding consumption during the period to ‘wealth’ at the end of the period and then subtracting ‘wealth’ at the beginning.”

Simons provides the following mathematical formula:

$$\text{HSI} = C + (NW_1 - NW_0)$$

Where:

- $\text{HSI}$ is the taxpayer’s income sources for the taxable period;
- $C$ is the market value of the taxpayer’s consumption for the period;
- $NW_1 - NW_0$ is the change in the market value of the taxpayer’s assets from the start of taxable period $(NW_0)$ to the end of that period $(NW_1)$.

---


Their formula for computing taxable income relies on two implicit assumptions about the taxable person and the taxable period:

- Income is being measured over some taxable period and that consumption and savings are being measured over the same period.
- Income is being attributed to some taxable person and that consumption and savings are being attributed to that same taxable person.

McIntyre\textsuperscript{14} states that without some such assumptions, the formula would be nonsensical. He suggests that to make those assumptions explicit, the Haig-Simons formula can be rewritten as follows:

\begin{equation}
HSI_{t,p} = C_{t,p} + (NW_t - NW_0)_{t,p}
\end{equation}

The assumptions made about the taxable person and the taxable period on the left side of the formula must be compatible with the assumptions made on the right side of the equation. However, it has been argued that income should be taxed when earned.\textsuperscript{15} The fact whether income is consumed or saved is not material. Every person’s accretion to wealth in any period falls within the tax base.

### 1.2 Statutory concept of income

#### 1.2.1 Overall Scheme of the Act

The concept of income that the Income Tax Act has is not the same that an economist has. An Income Tax Act that was drafted on economic concept would not work because many increases in wealth are not realised. Core provisions in Part B of the Act set out the key principles and presumptions on which all other parts are based. They are intended to impose tax liability, set out procedures that taxpayers must follow to calculate and satisfy their tax liability. Section BB 1 of the Act imposes tax liability by stating:

*Income tax is imposed on taxable income, at the rate or rates of tax fixed by an annual taxing Act, and is payable to the Crown under this Act and the Tax Administration Act 1994.*


The flowchart B2 of the Act ‘calculating and satisfying income tax liability’ provides the process that must be followed by taxpayers to calculate and satisfy their income tax liability for a year. The second page of this flow chart is reproduced below:

All taxpayers must calculate and satisfy their income tax liability in accordance with s BC 2 to s BC 6. Assessable income is defined in s BD 1. A taxpayer’s assessable income is any income which is not exempt income, excluded income or foreign sourced income of a non-resident. When a taxpayer’s assessable income is allocated to a particular income year it becomes annual gross income. [s BC 2]. The general rule is that items of income must be allocated to an income year in which they are derived. Deductions are defined in s BD 2. When taxpayer’s deductions are allocated to a particular income year it becomes annual total deduction [s BC 3]. The general rule is every deduction must be allocated to an income year in which the expenditure or loss is incurred. If for an income year a taxpayer’s annual gross income is more than the total

---

16 Subpart BC of the Act.
annual deductions the difference is their net income for the year [s BC4 (1)]. If for an income year a taxpayer’s annual gross income is less than the total annual deductions the difference is their net loss for the year, and their net income for the year is zero [s BC 4(3)]. A taxpayer with a net loss for an income year may, in accordance with Part I of the Act:

(a) subtract the net loss from their net income for a future year; or
(b) make the net loss available to another taxpayer to subtract from that other taxpayer’s net income for that or a future tax year [s IA 2].

A taxpayer’s taxable income for an income year is determined by subtracting any available net losses that the taxpayer has from their net income in accordance with Part I [s BC 5]. Gross income is the basis of the tax return. All taxable income was originally gross income but because deductions are subtracted from gross income, in the process of calculating taxable income, not all gross income is taxable.

1.2.2 The concept of income

Section YA 1 of the Act refers to s BD 1 (1) of the Act for the definition of income. Section BD 1(1) provides that: “an amount is income of a person if it is their income under a provision in Part C (Income).” Part C of the Act contains a number of specific provisions outlining what is included in the term income for income tax purposes. It also defines amounts that would be income nevertheless exempt or excluded from income. Amounts that are not included as income under Part C are not subject to income tax.

The assessment of income from personal exertion to tax rests primarily upon the inter-relationship of number of key sections in the Act. The pivotal section is section CA 1.

Section CA 1 of the Act states:

Amounts specifically identified

(1) An amount is income of a person if it is their income under a provision in this Part.

Ordinary meaning

(2) An amount is also income of a person if it is their income under ordinary concepts.
Section CA 1(1) sets out specific categories of income: Employment income, Business income, Income from property (Personal property, Real property) and Accrual income. These are not comprehensive, however if a receipt is not listed as a specific category it still falls to be considered whether a particular receipt is income according to the ordinary concept as per s CA 1(2) of the Act. Section CA 1 (2) is the statutory mechanism to incorporate the economists’ view of income that every person’s accretion to wealth in any period falls within the tax base.

In 2004, the Inland Revenue Department published an article titled “Income Tax Act 2004”, stating various aspects of different parts of the Income Tax Act 2004 (hereinafter referred to as ‘2004 Act’). The article stated that Part C contained, “An exhaustive list of provisions that state the circumstances in which a transaction or other event gives rise to income”. The Inland Revenue noted that section BD 1(1) ITA 2004 “identifies that Part C is a code in relation to its role of determining whether an amount arising from a transaction or event is income”. Against this, Alley and Maples commented that the Inland Revenue statement does not give the complete picture and there is no actual definition outlined in the 2004 Act.

In their view, section CA 1(2) of the 2004 Act acted as a “catch all” provision, providing that amounts that were not specifically referred to in that legislation could still constitute income according to ordinary concepts and be taxed under Part C. Section CA 1(2) is the most important provision in the Act. Some charging provisions

---


precede it, and (rather more) follow it. Other commentators on the reach of Part C have noted that since it: “includes ‘income under ordinary concepts’, what is (and what is not), income remains to a large extent a matter of common law principle.”

Across the Tasman, the Australian ITAA 1997 is of little assistance. ITAA 1997 section 6-5 (2) brings to tax net assessable income derived by Australian residents. Assessable income consists of “ordinary income” and “statutory income” (s 6-1(1) ITAA 1997). Ordinary income consists of income according to ordinary concepts from any source (s 6-5(5) ITAA 1997). Section 6-5(4) ITAA 1997 provides that a taxpayer is taken to have received an amount of ordinary income as soon as it is applied or dealt with in any way on the taxpayer’s behalf or as the taxpayer directs. So the ITAA 1997 also does not define the concept of income according to ordinary concepts or the concept of derivation. But section 6-5(4) ITAA 1997 is an umbrella provision. It ensures that nothing that is income according to the ordinary meaning of the word escapes tax.

---

23 Ibid.


25 Part 3 of the paper undertakes a review and analysis of the leading cases from Australia and United Kingdom. United Kingdom Income Tax Act is Schedular and there is no provision equivalent to s CA 1(2).

Part 2

Analytical Framework

2. Nature of Receipt

There are many ways in which a taxpayer can receive payments in personal capacity which result from a direct or an indirect employment relationship. In general the characterization of such receipts as capital or revenue is controversial. Items which are clearly gross income are for example wages, salaries, commissions and bonuses. Items which are clearly not gross income are for example reimbursement of expenses incurred by the employee on behalf of the employer and gifts which can be explained by some event clearly external to the employment relationship (such as a wedding gift). There is a distinction between receipts that are income and then, within the not income category, there are receipts that are not income because they are capital in nature and receipts that are not income for another reason, for example, gifts. For example the present given by a parent to a child is certainly a gain to the recipient but a pure gift and not income. Lotto or raffle winnings or a reward by the police or by the owner for finding stolen goods is not income for other reasons.

As mentioned earlier there are two ways to analyse gifts from personal exertion income:

(1) Ordinary concepts (s CA 1(2)) includes employment income (s CE 1) and business income (s CB 1); or

(2) Ordinary concepts (s CA 1(2)), employment income (s CE 1) and business income (s CB 1) are disparate tests.

To analyse gifts from personal exertion, this section develops the analytical framework for the concept of income, considering specifically, s CA 1 (2), s CE 1 and s CB 1 of the Act.

---


2.1 Ordinary Income

As discussed in part 1 of the paper, section CA 1(2) of the Act functioned as a “catch all” provision, providing that amounts that were not specifically referred to in that legislation constituted income under ordinary concepts.

The Act did not define “income” and it was therefore left to the courts and to commentators to arrive at a sustainable meaning.29 Therefore, taxpayers and their advisors together with the Inland Revenue have had no choice but to work within the ambit of such a limited concept of income.30 The New Zealand courts have relied on cases from other jurisdictions in order to derive a general concept of income. In Scott v Commissioner of Taxation, Jordan CJ concluded31 that the word “income” was not a term of art and that what forms of receipt were comprehended within it and what principles were to be applied in ascertaining which of these receipts ought to be treated as income must be determined in accordance with the ordinary concepts and usages of mankind except in so far as the statute stated or indicated an intention that receipts which were not income in ordinary parlance were to be treated as income, or that special rules were to be applied in arriving at the taxable amount of such receipts. 32

Holmes notes that the Courts when determining income for tax purposes “refer to adoption of the ‘ordinary’ or ‘natural’ meaning, or the ‘customary usage’ of the word income”.33 He noted that to constitute income receipts require “the presence of: An

29 The judicial approach to identification of income is different from the economic concept.


32 In A Taxpayer v CIR (1997) 18 NZTC 13,350 (CA) when the Inland Revenue Department was relying on American and Canadian Courts economic concept Richardson J at page 13,556 commented: “The approach taken to the reach of taxes over income in other jurisdictions with their different economies and with different assumptions as to the influence of property and other concepts in the making of gains is not necessarily a sound basis for determining the scope and application of the New Zealand legislation. Thus, the United Kingdom of 200 years ago when income tax was first introduced was very different from the pioneering, entrepreneurial, less static and more mobile United States of 1913. The American cases on which Mr McKay drew need to be read in their economic and social context.” The Court of Appeal rejected any reliance upon the economic reality of the situation and based its decision upon the application of property and trust concepts. Richardson J at page 13,359 stated: “…there is no gain to a taxpayer unless the receipt is derived beneficially by the taxpayer. Taxation by economic equivalence is impermissible.” Hence the substance approach is not relevant for tax purposes.

incoming or inflow; Convertibility into cash; Periodicity or recurrence; A reward from employment or vocation or property; Realisation; Separation from source; A profit-making purpose, and conformity with the “ordinary” meaning of income.”

Ohms notes that “ordinary income is the residue of receipts and outgoings that result from a transaction, scheme or undertaking entered into by a taxpayer with the purpose or intention of making a profit or gain. A transaction or a scheme includes the carrying on of a business, an employment relationship or the use of property.”

Professor R Parsons identified some propositions which provide the hallmarks of income according to ordinary concepts. Parsons noted that the concept of income denotes two component parts. First, there must be a gain by the taxpayer. Second, once a gain has been established, there must be something which comes in. The second component relates to the concept of derivation. So first of all, a gain with an income character must be identified and then once identified, a determination needs to be made about whether it has been derived by the relevant taxpayer. Parsons definitive text makes number of assertions, or propositions, which can be used in a general way to identify receipts as income.

The main “criteria” needed to satisfy the judicial concept of income are:

- Realisation – gain must be derived;
- Gain must be “revenue” in nature;
- Capital gains are excluded; and
- Windfall gains are excluded.

References:
2.1.1 Realisation – gain must be derived

Holmes observes that a gain must be realised (come in) before it can be treated as income in the legal sense. Parsons suggests that: “An item is income of a taxpayer, in the amount of its realisable value, if it has been derived by him and the item is a gain derived in circumstances which give it in other respects an income character”. The concept of gain is therefore seen as an important element in Parsons’ idea of the tax law concept of income. Conceptually, income derivation is a hard area. Writing about the concept of income derivation, Sir Ivor has noted the fact that the judicial concept of income must work in the real world.

Section BD 3 of the Act provides that assessable income must be allocated to the income year in which the amount is derived by the taxpayer and section BC 5 provides that income tax is imposed on the taxable income derived by the taxpayer during the income year. The term “derived” is not defined in the Act. The Act does not set out any procedures that a taxpayer must follow to determine the amount of income derived by them. The Oxford English Dictionary defines the word ‘derive’ as meaning “to draw, fetch, get, gain, obtain (a thing from a source).” The word ‘derived’ is not necessarily equivalent in meaning to ‘earned’. In Brent, Gibbs J said: “It has become well established that unless the Act makes some specific provision on the point the amount of income derived is to be determined by the application of ordinary business and commercial principles and that the method of accounting to be adopted is that which is calculated to give a substantially correct reflex of the taxpayer’s true income”.


43 Brent v FCT (1971) 125 CLR 418, at p 423.

44 Brent v FCT (1971) 125 CLR 418, at p 429.
In *Brent* the wife of a train robber sold her life story to a newspaper for its exclusive publication for $65,250. She received $10,000 on the signing of the agreement in the 1970 income year. The remaining amount was paid to her in a later income year on the signing of the manuscript containing her life story. She was held to have derived assessable income when she received money for the signing of the agreement to a newspaper for its exclusive publication. Gibbs J at the High Court of Australia noted that her income for the 1970 income year was $10,000, the amount realised by her and not the amount she sold her story for. He said that there is no commercial practice, or principle of accountancy, that requires the total earnings from personal services to be recognised in a year in which it was earned but not received. Furthermore, she did not carry on a business or profession and she had no stock-in-trade and was not likely to start writing off bad debts. Her expenditure did not correspond with, or materially contribute to, her earnings. Gibbs J further said that the accepted method of accounting for business and trading concerns had no application to her situation.

Section BD 3(4) of the Act provides that employment income is derived when it is credited in the employee’s bank account. In Carden’s case Dixon J noted: “Speaking generally, in the assessment of income the object is to discover what gains have during the period of account come home to the taxpayer in a realized or immediately realizable form.”

In *Arthur Murray (NSW) Pty Ltd* the prepayments made for dancing tuition which could extend beyond the current year were held to be income in the year that the lessons were provided and not in the year the fees were paid. In *Arthur Murray* the court observed: “It refers to amounts which have not only been received but have ‘come

---

45 *Brent v FCT* (1971) 125 CLR 418, at p 429.

46 *Brent v FCT* (1971) 125 CLR 418, at p 430. This was cited from Commissioner of Taxes (S.A.) v. Executor, Trustee and Agency Co. of South Australia Ltd. (Carden’s Case) (1938) 63 C.L.R.108, at pp. 152-154.

47 In *Case D 14* (1979) 4 NZTC 60,507, an accountant was paid a salary for services to be performed the following year. The Taxation Review Authority held that the salary was derived by an accountant in the year he received it.

48 Commissioner of Taxes (S.A.) v. Executor, Trustee and Agency Co. of South Australia Ltd. (Carden’s Case)) (1938) 63 C.L.R.108, at p155.

49 *Arthur Murray (NSW) Pty Ltd v FCT* (1965) 114 CLR 314.

50 Ibid, at p 318.
home’ to the taxpayer; and that must surely involve, if the word ‘income’ is to convey the notion it expresses in the practical affairs of business life, not only that the amounts received are unaffected by legal restrictions, as by reason of a trust or charge in favour of the payer - not only that they have been received beneficially - but that the situation has been reached in which they may properly be counted as gains completely made, so that there is neither legal nor business unsoundness in regarding them without qualification as income derived.”

‘Convertibility into cash’ and ‘realisation’ are not synonymous concepts. Lord Traynor in Californian Copper Syndicate v Harris stated:51 “a profit is realised [and therefore taxable under schedule D of the United Kingdom Income Tax Act 1842] when the seller gets the price he has bargained for. …[I]f there can be no realised profit, except when that is paid in cash, the shares were realisable and could have been turned into cash, if the Appellants had been pleased to do so.”

Holmes52 notes that realisation connotes a change in the form of an accrued gain from one type of asset to another and it may or may not occur subsequent to the recognition of economic income.

2.1.2 Gain must be “Revenue” in Nature

The Act defines the concept of revenue on the basis of its natural and ordinary meaning. Ultimately it is a matter of commonsense. In ascertaining whether a gain constitutes income, tax law has focused on gains made from services rendered,53 the carrying on of a business54 or from property.55 These gains were recognised as being of

51 Californian Copper Syndicate (Limited and Reduced) v Harris (1904) 5 TC 159, at p 167-168. In April 1902 a parcel of land was sold by the taxpayer with the balance being disposed of in August 1904, the consideration for the transactions being 300,000 in fully paid up shares in the purchaser company. Taxpayer claimed it had merely substituted one form of investment for another.


53 ITA 2007, s CA1, s CE 1

54 ITA 2007, s CB 1.

55 ITA 2007, ss CB 3 - CB 5.
an income nature and thus taxable. Interest, rents, dividends and royalties are generally recognised as having the character of income.\(^56\)

The general concept of net income is based on identification of transactions which give rise to net income. Richardson P in *A Taxpayer* observed:\(^57\) “Again, income is a flow of money or money’s worth, a series of periodic receipts arising from the ownership of property or capital, or from labour, or a combination, eg rent, interest and dividends, salary and other personal exertion receipts, annuities and business receipts.”

As the tax law concept of income evolved, the courts identified a number of common elements that were present in established types of income. However, an all encompassing definition has not yet been developed, partly due to the fact that, as Cooper et al.\(^58\) stated, judicial pronouncements will always be subject to varied interpretations. Holmes\(^59\) also concluded that the distinction between income and non-income receipts and benefits turned on statutory interpretation.

The distinction between an income receipt which will be liable to tax and a capital receipt which will not is thus a fundamental concept underpinning the New Zealand Income Tax legislation. The cases which come before the courts are those in which a receipt does not lie clearly on one side or the other of the capital or not income for other reasons/revenue line. The courts will then turn to established indicia of the presence of income or otherwise. In *Scott v Commissioner of Taxation*, Jordan CJ observed:\(^60\) “the word “income” appears “on both sides of the equation”. The definitions, however, did serve to flag the fact that property and personal exertion represented, at the very least, the principal sources from which income may be said to be derived.”  


\(^{60}\) *Scott v Commissioner of Taxation* (1935) 3 ATD 142 at 145; (1935) 35 SR (NSW) 215, at p 220.
Macomber, the United States Supreme Court attempted to put forth such a general concept of income. The case is well known for the analogy put forth by Pitney J. where revenue was seen as the fruit or produce (e.g., dividends, rents, royalties) and capital as the tree or the enduring source (e.g., land, or other property) from which the revenue is able to be derived (or a taxpayer ability to earn revenue from personal exertion).

However, it should be noted that the concept of income advocated by Pitney J. includes gains from the sale of assets. Krever has noted that the fruit and tree metaphor has been so edited and taken out of context by lawyers and writers as to give an entirely different meaning to that which was intended. He then goes on to state that Eisner v Macomber stands for the principle that both income and realised capital gains constitute income for income tax purposes.

New Zealand tax legislation did not evolve with the above concept. Unlike the United States, in New Zealand profits made upon the realisation of an asset do not constitute income for income tax purposes. Lord Justice Clerk and Lord MacDonald in California Copper Syndicate v Harris stated:

“That where the owner of an ordinary investment chooses to realise it, and obtains a greater price for it than he originally acquired it at, the enhanced price is not a profit in the sense of Schedule D of the Income Tax Act 1842.”

They further stated that where what is done constitutes the carrying on or out of a business; profits from the realisation of the asset may be assessable. Motive of the recipient must be considered. According to Lord MacDonald the question to be asked was, “is the sum of gain that has been made a mere enhancement of value by realising a

---

61 Eisner v Macomber (1919) 252 US 189. The Supreme Court of the United States of America in Eisner v Macomber said that; “The fundamental relation of “capital” to ‘income’ has been much discussed by economists, the former being likened to the tree or the land, the latter to the fruit or the crop: the former being depicted as a reservoir supplied from springs, the latter as the outlet stream, to be measured by its flow during a period of time ...”.


64 Ibid.

65 California Copper Syndicate v Harris (1904) 5 TC 159, at p 165.
security, or is it a gain made in the operation of business in carrying out a scheme for profit making?\(^66\) A receipt may constitute income if it arises from an isolated business operation or commercial transaction entered into otherwise than in the ordinary course of the carrying on of the taxpayer's business, so long as the taxpayer entered into the transaction with the intention or purpose of making a relevant profit or gain from the transaction.

In *Myer Emporium*\(^67\) the fact that the lump sum received in consideration of the assignment was outside the ordinary trading activities of Myer was not disputed by the High Court of Australia. However, the court did not view this finding as a bar to the finding that the sum received could not be taxed. The court stated that if the circumstances are such as to give rise to the inference that the taxpayer's intention or purpose in entering into the transaction was to make a profit or gain, the profit or gain will be income notwithstanding that the transaction was extraordinary judged by reference to the ordinary course of the taxpayer's business. Nor does the fact that a profit or gain is made as a result of an isolated venture or a single “one-off” transaction precludes it from being properly characterised as income.\(^68\)

In *A Taxpayer V CIR* Richardson P said: \(^69\) “A further underlying notion is the idea of gain from the carrying on of an organised activity – an employment, a business or profession, an adventure in the nature of trade, or a business deal - directed to the making of gain.”\(^{emphasis added}\) Sums which are received annually or periodically are often revenue nature but that factor is an evidential test not a decisive test in determining the revenue nature of the sums.\(^70\) It is necessary to look at the primary purpose for which the amount is received.\(^71\)

---

\(^{66}\) *California Copper Syndicate v Harris* (1904) 5 TC 159, at p 166.

\(^{67}\) *FCT v The Myer Emporium Ltd* 87 ATC 4,363.

\(^{68}\) *FCT v The Myer Emporium Ltd* 87 ATC 4,363, at p 4,366 – 4,367.

\(^{69}\) *A Taxpayer v CIR* 1997)18 NZTC 13,350, at p 13,355.


\(^{71}\) The origin of this test is *Valambrosa Rubber Co Ltd V Farmer (Surveyor of Taxes)* (1910) 5 TC 529.
Tax law has recognised the ability to tax personal exertion receipt as being dependent upon the nature of the receipt. The nature of a receipt is thus determined by the circumstances of the recipient. In *Hobbs v Hussey*, Mr Hobbs, a notorious criminal, entered into a contract with a newspaper to write a series of articles about his ‘life in crime’ in exchange for a payment of certain amount. Mr Hobbs sold the copyright in the articles, which had not been written at the time the contract was entered into. Lawrence J. held that the true nature of the transaction was the performance of services and that the profits were of a revenue nature. He further noted that the sale of the copyright was merely ancillary and did not affect the true nature of the transaction. He stated: “the performance of services, although they may involve some subsidiary sale of property (e.g. dentures sold by a dentist) are in their essence of a revenue nature since they are the fruit of the individual’s capacity which may be regarded in a sense as his capital but are not the capital itself.”

In *G v CIR* the Supreme Court was required to determine the assessability of gifts made to the taxpayer, an evangelist. McCarthy J held that gifts which were related to the income producing activities of the taxpayer were assessable. Those gifts were received periodically with a profit making purpose or intent. In this case the gifts were received by the taxpayer in anticipation that they will be a means of support for him. In *Reid V CIR* considering whether the student allowance was assessable to the taxpayer, Richardson J observed: “If it has that quality of regularity or recurrence then the payments become part of the receipts upon which the recipient may depend for his living expenses, just as in the case of a salary or wage earner, annuitant or welfare beneficiary. But that in itself is not enough and consideration must be given to the relationship between payer and payee and to purpose of the payment, in order to determine the quality of the payment in the hands of the payee.”

---


73 Ibid, at p 496.

74 *Graham* v *CIR* [1961] NZLR 994.

75 *Graham* v *CIR* [1961] NZLR 994, at p 999.

Therefore it is submitted that to determine whether a receipt from personal exertion would be considered as income, the evidential tests applied by the courts are: a gain is derived by a person for services rendered, periodicity, recurrence or regularity, an expectation of reward and the intention of the donor and the donee.77

2.1.3 Capital Gains are Excluded

The default rule of New Zealand tax law (s BD 1(1) of the Act) is that capital gains, whether realised or unrealised, are not taxable in the hands of the recipient despite representing a gain to that person. However, many types of capital gains, which prima facie are not taxable, are being drawn into the tax base by virtue of particular legislative provisions.78

Ohms notes, “An amount will be a capital gain if it results from a transaction, scheme or undertaking entered into by a taxpayer with the purpose or intention of creating, enhancing or disposing of the setting or structure which enables the profit or gain to arise.”79 Ohms assumed that the state of mind test applies to determine whether a receipt is a capital gain.80 If a transaction is a part of income earning structure and is not entered into with a profit making purpose or intention it will be capital gain.

According to Richardson and Cooper et al.81 trust law concepts of income have been influential in shaping the tax law concept of income. Cooper et al.82 cited an example of the exclusion of capital gains from the tax law concept of income as having its origins in trust law, which recognised a difference between those beneficiaries


78 Sections CB 6 to s CB 23 of ITA 2007 contain a series of provisions to catch land sales.


entitled to receive income from the property and those beneficiaries entitled to receive the property itself.

The treatment of increases in capital as constituting a profit or gain under the United Kingdom Income Tax Act 1918 was considered in *Ryall v Hoare* where Rowlatt J. concluded that:

“… a capital accretion is outside the words “profits or gains”, as used in these Acts”. Therefore, profits made from the isolated buying and selling of an item fell outside the scope of income/gain as per Rowlatt J’s idea of income.

### 2.1.4 Windfall Gains are Excluded.

Section BD 1(1) of the Act provides that windfall gains are not income and are therefore not taxed. Ohms states an amount will be a windfall gain if it results from a transaction, scheme or undertaking entered into by a taxpayer with neither the purpose nor intention of making a profit or gain nor of creating, enhancing or disposing of the setting or structure which enables the profit to arise. He assumed that the state of mind test applies to determine whether a receipt is a windfall gain. A windfall gain neither relates to the income earning process nor to the framework which enables the income activity to take place. It is never received with a profit making purpose.

Alley and Maples observe that there is an overlap between the terms “windfall gain” and “gift”. They believe that windfall gains may not be earned but arise by virtue of luck and payments made by way of personal esteem or testimonial are gifts. Ross and Burgess refer to a gift as a windfall payment.

---


85 *Scott v FCT* [1967] ALR 561.


87 Ibid.

In *G v CIR* the Supreme Court adopted the position of English law and observed that: 89 “Though gratuitous payments amount to income in the widest sense of the word – namely something which comes in – it has generally been accepted that they are not part of the taxpayer’s assessable income unless they can be shown to be embraced by some specific provision of the tax law which makes them taxable.”

Therefore, each gift is considered on its own facts. Only those gifts which are related to the income producing activities of the taxpayer are assessable, and mere personal gifts made purely as a mark of affection, esteem or respect are not.

The judicial concept adopted by the New Zealand courts had its origins in the interpretation by the English courts of the English tax legislation which only imposed tax on receipts which had a source specified in the Schedules. While interpreting the Schedules the courts applied similar principles to those that had been used in trust law but the trust concept was not simply adopted for tax purposes. Therefore, gifts were excluded from the tax net unless they could be brought within the wording of the legislation. Ross and Burgess stated: 90 “[w]hy [the courts exclude gifts from income] has never been clearly explained in the case law, but perhaps the isolated nature of these receipts, their general unpredictability and lack of control the recipient has over their derivation qualifies gifts for special treatment.” However, Ross and Burgess’s justification based on particular characteristics of a gift do not provide a complete answer. In *FCT v Squatting Investment Co Ltd* Kitto J commented as follows: 91 “the test of whether a ‘gift’ is income in the ordinary sense of the word is whether it is ‘made in relation to some activity or occupation of the donee of an income-producing character’.” According to the income and non-income distinction developed by the English courts, 92 a gift is not a reward for a donee’s labour in an office or employment. Nor is the gift a product of the donee’s property. A gift might also be viewed as a

---


91 *FCT v. Squatting Investment Co Ltd* (1953) 86 CLR 570, at p 633.

92 Income must be coming; Income must be convertible into money or money’s worth; Income must generally comprise a periodic or recurrent flow; Income must be reward or effort or the produce of property.
distribution of the donor’s income or property rather than an income receipt of the donee.

2.2 Section CE 1 Employment Income

Payments to an employee constitute payments of salary or wages which are subject to the PAYE system. For a payment (employment income) for personal exertion to constitute a payment of salary or wages it must be paid on account of an employment relationship. The term “employment relationship” is not defined in the Act. However, income from an employment relationship is captured by s CE 1 of the Act: “Amounts derived in connection with employment.”

Section CE 1 provides: The following amounts derived by a person in connection with their employment or service are income of the person:

(a) salary or wages or an allowance, bonus, extra pay, or gratuity: expenditure on account of an employee that is expenditure on account of the person;
(b) the market value of board that the person receives in connection with their employment or service:
(c) a benefit received under a share purchase agreement:
(d) directors’ fees:
(e) compensation for loss of employment or service:
(g) any other benefit in money.

The words used in the Act, “amounts derived by a person in connection with the employment or service of the person” allows the inclusion in income, benefits in

93 ITA 2007. Section CE 1 includes all employment income.

94 ITA 2007.

95 Section YA 1 defines wages or salary as any salary, wages, or allowances relating to the employment of a person including all sums received or receivable by way of overtime pay, bonus, gratuity, extra salary, commission or remuneration of any kind. It includes periodic payments by way of superannuation, pension, retiring allowance or any other allowance or annuity payable in respect of or in relation to the past employment of the taxpayer or of any person of whom the taxpayer was the spouse, child or dependent.

96 Section CE 5 defines expenditure on account of an employee as reimbursement of expenditure incurred by an employee on behalf of the employer. The receipt is not taxable.

97 ITA 2007, s CE 1. Naismith v CIR (1981) 5 NZTC 61,046 is the authority for this proposition.
money derived in connection with employment.\textsuperscript{98} The words refer to an existing employment or service, and cannot be treated as extending to an employment or service which has come to an end. An employment income is derived at the point that it is earned. The tax on that income is paid at that time. The case of \textit{Hadlee and Sydney Bridge Nominees Ltd} \textsuperscript{99} offers an example of this approach. In that case Richardson J said:\textsuperscript{100}

“In relation to employment income the whole PAYE structure proceeds on the premise that income of that kind is derived by the employee concerned. That is reflected in the definition of salary or wages (sec 2)[\textsuperscript{101}] and source deduction payments (sec 6)[\textsuperscript{102}]; and in the respective duties of employers and employees in relation to tax deductions by employers from salary, wages and other source deduction payments, the crediting of those deductions and the assessment and payment of tax under Pt XI of the Act.[\textsuperscript{103}] The statutory scheme in that regard does not allow for the possibility of diversion of that income by means of any kind of antecedent arrangement before its derivation by the employee.

Employment income is an amount which is a reward for services. The \textit{A Taxpayer} \textsuperscript{104} case offers an example to this approach. In \textit{A Taxpayer} an accountant systematically embezzled over $2 million from his employer, which he used to speculate in the futures market. Unfortunately his future trading was not successful and he made losses. Eventually he was caught and had to repay the funds embezzled, of which he could repay only half. The Commissioner assessed him on the funds stolen and income from his trading activities. In reaching his decision whether moneys stolen by an employee from his employer were assessable to the employee as monetary remuneration under s 65(2)(b) of the 1976 Act\textsuperscript{105} Tipping J said: \textsuperscript{106}

\textsuperscript{98} The employee is taxed on income derived, employee expenses discharged by the employer and non-cash benefits from the provision of accommodation and share investments.

\textsuperscript{99} \textit{Hadlee and Sydney Bridge Nominees Ltd v C of IR} (1991) 13 NZTC 8,116.

\textsuperscript{100} Ibid, at p 8,128.

\textsuperscript{101} Equivalent to s RD 5 of the 2007 Act.

\textsuperscript{102} Equivalent to s RD 3 (1) – (4) of the 2007 Act.

\textsuperscript{103} Equivalent to Part R of the 2007 Act.

\textsuperscript{104} \textit{A Taxpayer v C of IR} (1997) 18 NZTC 13,350.

\textsuperscript{105} Equivalent to s CE 1 of the 2007 Act.
“I agree with Morris J that while the employment relationship provided the setting and the opportunity for the thefts, that is as far as it goes. The clear connotation of the phrase ‘monetary remuneration’ and the statutory definition is one of consensual payments by employer to employee. It is a rather bizarre idea to suggest that when an employee fraudulently helps himself to his employer’s money, this is monetary remuneration. It is theoretically possible to fit stolen money within the definition by saying that the money is a ‘benefit in money ... in respect of or in relation to’ the taxpayer’s employment. But I cannot accept that this is an appropriate conclusion. It is not, in my judgment, the sort of ‘benefit in money’ contemplated by the definition.”

The Australian Income Tax Assessment Act 1997 (ITAA 1997) s 15(2) states: “in respect of, or for, or in relation directly or indirectly to any employment of or services rendered by him”. This similarity in wording allows greater reliance on the Australian cases than the English cases. Molloy suggests that they cannot be relied on without taking this difference into account. Similarly the United Kingdom Income Tax Act is scheduler and the NZ Income Tax Act is global gross.

Employment relationship relies on general law. Consequently, this involves drawing a distinction between an employee and an independent contractor, a distinction which is difficult to draw in practice.

2.2.1 Employee v Independent Contractor

An employee is defined in section 6 of the Employment Relations Act 2000 (ERA 2000). Under s6(1) an: “employee ... means any person of any age employed by an employer to do any work for hire or reward under a contract of service ...”. Section 5 of

---

107 Section 15-2(1) ITAA 1997: Assessable income includes the value to the taxpayer of all allowances, gratuities, compensation, benefits, bonuses and premiums provided in respect of, or for or in relation directly or indirectly to, any employment of or services rendered by the taxpayer (including any service as a member of the Defence Force). Equivalent to section 26(e) ITAA 1936.
108 See AP Molloy, Molloy on Income Tax, Butterworths, Wellington, 1976 p 503 and accompanying text for further discussion of the difference in reliance on English and Australian cases. Schedule E to the Income Tax Act 1952 states: “in respect of any office employment or pension, the profits or gains arising or accruing from which ...”. The payments come within Schedule IX, which referred, in respect of an office or employment of profit mentioned in Schedule E, to “all salaries, fees, wages, prerequisites or profits whatsoever therefrom”.

30
the ERA states that an “employment agreement means a contract of service”. The term contract of service is taken from the common law and is used to distinguish the status of an employee from other types of ‘worker’. The common law uses a similar term – contract for services - to describe the status of other types of worker such as the self employed or independent contractors.

Section 6 of the ERA 2000 provides that, in deciding whether a person is employed by another person under a contract of service for the purposes of that Act, the Employment Court or the Employment Relations Authority (as the case may be) must determine the real nature of the relationship between them. The court or the authority must consider all relevant matters, including any matters that indicate the intention of the persons, and is not to treat as a determining matter any statement by the persons that describes the nature of their relationship.\(^\text{109}\)

In its first employment law decision, \textit{Bryson v Three Foot Six Ltd},\(^\text{110}\) New Zealand Supreme Court has ruled on the interpretation of s 6 ERA 2000, which determines if a worker is an employee or a contractor.

From April 2000 to September 2001, Mr Bryson worked for Three Foot Six Limited as a set model technician on the Lord of the Rings production. When he was made redundant, his unjustifiable dismissal action was unsuccessfully opposed in the Employment Authority on the grounds that he was an independent contractor. A de novo hearing in the Employment Court found Mr Bryson to be an employee but this judgment was reversed by the Court of Appeal decision that he was a contractor. The Supreme Court restored the Employment Court’s judgment, affirming Mr Bryson to be an employee. This allowed him to return to the Authority to have his personal grievance heard.

\[^{109}\text{Inland Revenue Department Tax Information Bulletin Vol 5:1, July 1993, p5 lists the five tests of employment status adopted by Inland Revenue. The five tests: control, organisation or integration, fundamental test, intention test and multiple test were listed in } \text{Enterprise Cars Ltd v CIR (1988) 10 NZTC 5,126 at p 5,131.}\]

\[^{110}\text{Bryson v Three Foot Six Limited (2005) 22 NZTC 19,242.}\]
In the Employment Court, Shaw, J\textsuperscript{111} summarized the principles established by two previous cases (\textit{Koia v Carlyon Holdings},\textsuperscript{112} and \textit{Curlew v Harvey Norman Stores}\textsuperscript{113}) in interpreting s 6 as:\textsuperscript{114}

- The court must determine the real nature of the relationship.
- The intention of the parties is still relevant but no longer decisive.
- Statement by the parties, including contractual statements, are not decisive of the nature of the relationship.
- The real nature of the relationship can be ascertained by analyzing the tests that have been historically applies such as control, integration, and the “fundamental” test.
- The fundamental test examines whether a person performing the services is doing so on their own account.
- Another matter which may assist in the determination of the issue is industry practice although this is far from determinative of the primary question.

The Supreme Court\textsuperscript{115} found that in this list “Shaw J accurately state[d] what the Court must do and list[ed] the matters which are relevant”.

The role of the traditional tests, (control, integration and the “fundamental” test), in determining the nature of an employment relationship was specifically affirmed by the Supreme Court. The Supreme Court found: \textsuperscript{116} “All relevant matters... clearly require[ ] the Court or the Authority to have regard to features of control and integration and to whether the contracted person has been effectively working on his or her account (the fundamental test), which were important determinants of the relationship at common law.” A prerequisite to applying these tests is to consider the terms and conditions of the contract and how it operates in practice.

\textsuperscript{111} \textit{Bryson v Three Foot Six Ltd} [2003]1 ERNZ 581; [2005] NZSC 34.

\textsuperscript{112} \textit{Koia v Carlyon Holdings Ltd} (2001) 6 NZELC 96,407.

\textsuperscript{113} \textit{Curlew v Harvey Norman Stores (NZ) Pty Ltd} [2000] 1 ERNZ 114.

\textsuperscript{114} \textit{Bryson v Three Foot Six Ltd} [2003]1 ERNZ 581, at para 19.

\textsuperscript{115} \textit{Bryson v Three Foot Six Ltd} [2005] NZSC 34, at para 32.

\textsuperscript{116} Ibid.
One of the Employment Court decision “principles” endorsed by the Supreme Court is that the intention of the parties is still relevant but no longer decisive. Intention is to be derived from “all relevant matters” including industry practice and a consideration of the agreements terms and conditions.\textsuperscript{117} It is open to the Employment Court to find on other sufficient evidence that common intention cannot be assumed on the basis of the wording of the agreement or of usual industry practice. Shaw, J\textsuperscript{118} found “[the] evidence [of] industry [practice] ... of little weight in the case before her because Mr Bryson’s working condition did not appear to be typical of the industry.”\textsuperscript{119}

Previously the law had a different emphasis. Under the Employment Contracts Act 1991, the Court of Appeal in \textit{Cunningham}\textsuperscript{120} held that it had to determine the true nature of the relationship by endeavouring to ascertain the intention of the parties and that where the parties had entered into a written contract at the outset of their arrangement the case would turn upon ‘the true interpretation and effect of the written terms’.

In the overturned Court of Appeal judgement in \textit{Bryson} the court appeared to be returning more to this emphasis. The majority of the Court of Appeal held that intention and the nature of the industry practice should be the decisive features in deciding on Mr Bryson’s employment status and that common law tests in themselves were not adequate to establish this. This finding has now been reversed by the Supreme Court. The Supreme Court decision in \textit{Bryson} reinstates a traditional, straight forward approach to determining employment relationship.

\textbf{2.2.2 History of s CE 1 of the Act}

To prevent the erosion of the tax base of the country, the sections of the New Zealand Income Tax Act which specifically make income from personal exertion assessable, have been amended from time to time. Section 88(1) (b) of the Land and

\textsuperscript{117} \textit{Bryson v Three Foot Six Ltd} [2005] NZSC 34, at para 35.

\textsuperscript{118} \textit{Bryson v Three Foot Six Ltd} [2003]1 ERNZ 581, at para 38.

\textsuperscript{119} \textit{Bryson v Three Foot Six Ltd} [2003]1 ERNZ 581, at para 9 Shaw J looked for “any mutual turning of minds to the true nature of his employment” and said that the assumptions of the employer about the employment status of the worker “ could not be taken as determinative.”

\textsuperscript{120} \textit{Cunningham v TNT Express Worldwide (NZ)Ltd} [1993]1 ERNZ 695, at p 701.
Income Tax Act 1954 specifically makes earnings from personal exertion assessable to income tax. The section states assessable income includes: “all salaries, wages, or allowances (whether in cash or otherwise), including all sums received or receivable by way of bonus, gratuity, extra salary [compensation for loss of employment], or emolument of any kind, in respect of or in relation to the employment or service of the taxpayer.” Later in 1968, section 88 C was introduced in the Land and Income Tax Act 1954, which overrode the old law by extending the meaning of “allowances” to include any benefit conferred on an employee under any share option or purchase scheme. In 1973 section 88(1)(b) of New Zealand Land and Income Tax Act 1954 was amended with the addition of “compensation for loss of office or employment as assessable income”. This immediately clarified the law and removed all uncertainty by making compensation payments for loss of office assessable to income tax. Section 88(1)(b), therefore immediately made remuneration for personal services derived from salaries, wages, commissions, fees and other payments that may be voluntarily made, such as bonuses and compensation payments for loss of employment assessable to income tax. This section together with a miscellaneous collection of other sections in the Land and Income Tax Act 1954 dealing inter alia, with retiring allowances paid to employees (s 88 B),121 with share purchase scheme (s 88 C) and with the provision of board lodging or housing by an employer (s 89), prima facie catch nearly all payments received by an employee in the course of his employment.

In the rewritten statute of 1976, section 65(2)(b) states assessable income of a person is deemed to include, “All monetary remuneration.” The definition of monetary remuneration includes:122 “Any salary, wage, allowance, bonus, gratuity, extra salary, compensation for loss of office or employment, emolument (of whatever kind), or other benefit in money, in respect of or in relation to the employment or service of the taxpayer; and includes any expenditure on account of an employee [but does not include any employer superannuation contribution].” In 1989 the definition of monetary remuneration of the Income Tax Act 1976 was amended by adding the words “but does not include any employer superannuation contribution.”

---

121 Section 88B replaces the proviso to s 88(1) (b) which prior to 1968 sparsely covered lump sum payments. Under the proviso only five percent of a lump sum retiring allowance was assessable to income tax.

122 The Income tax Act 1976, s 2.
(i) Any expenditure on account of an employee:

(ii) Any benefit of a kind referred to in section CH 2.\(^{123}\)

(iii) In the case of a taxpayer who in any income year has been provided in respect of any office or position held by the taxpayer with board or lodging, or the use of a house or quarters, or has been paid an allowance instead of being so provided with board or lodging or with the use of a house or quarters, the [market] value of those benefits; and the value of the benefits shall be determined in case of dispute by the Commissioner;

but does not include any employer superannuation contribution.”

In 1996 section BB 4(b) of the Income Tax Act 1994 was replaced as s CH 3.\(^{124}\) In 2001 the definition of monetary remuneration was amended by inserting in para (a) (iii) “market”. Income Tax Act 1994 was also amended in 2001 to include restrictive covenants and exit inducement paid to employees or contractor as assessable income.\(^{125}\)

In the rewritten statute in 2004 section CE 1 states:
The following amounts derived by a person in connection with their employment or service are income of the person:

(a) Salary or wages or an allowance, bonus extra pay or gratuity[:]

(b) Expenditure on account of an employee that is expenditure on account the person[:]

(c) the market value of board that the person receives in connection with their employment or service[:]

(d) a benefit received under a share purchase agreement[:]

(e) director’s fees[:]

(f) compensation for loss of employment or service[:]

(g) any other benefit in money.

---

\(^{123}\) Section CH 2 states Monetary remuneration “includes any benefit (determined in accordance with this section) conferred on any taxpayer in respect of, or in relation to, or in the course of, or by virtue of, the taxpayer’s employment or service, or future employment or service, under any agreement, entered into on or after 19 July 1968, to sell or issue shares in any company to the taxpayer.”

\(^{124}\) Taxation (Core Provisions) Act 1996.

\(^{125}\) Section CHA 1 and s CHA 2 were inserted in the Income Tax ACT 1994 with application to amounts derived on or after 27 March 2001. Section CHA 1 and s CHA 2 is equivalent to s CE 9 and s CE 10 of the Income Tax Act 2007.
The words “in respect of or in relation to the employment or service of the taxpayer” of the 1994 statute had been replaced in the rewritten statute in 2004 and 2007 as “in connection with their employment or service”. The word emoluments which appeared in Section 88(1) (b) of the Land and Income Tax Act 1954 and in the Income Tax Act 1976 via the definition of “monetary remuneration” had been dropped from s CE 1 of the Act. Section OE 4(1)(c) of the 2004 Income Tax Act\(^\text{126}\) and its cross-reference to section CE 1 states: “all salaries, wages, allowances, and emoluments of any kind earned in New Zealand in the service of any employer or principal, whether resident in New Zealand or elsewhere:” will have a source in New Zealand. However, section YD 4(4) of the 2007 Act\(^\text{127}\), and its cross-reference to section CE 1 states: “An amount that is income under section CE 1 (amounts derived in connection with employment) has a source in New Zealand if the amount is earned in New Zealand, even if the employer is not a New Zealand resident”, it will have a source in New Zealand.

The effect of the changes in the 2007 Act is to remove a direct reference to “emoluments” from the source rules which existed up until and including the 2004 Act. The term “emoluments” is very wide concept and could well catch a number of personal exertion income discussed in this paper.

2.3 Section CB 1 Business Income

Section CB 1\(^\text{128}\) of the Act states that an amount that a person derives from a business is income of the person.\(^\text{129}\)

“Business” is defined in s YA 1, inter alia to include any profession, trade or undertaking carried on for profit.

The word ‘manufacture’ and ‘pecuniary’ has been dropped from the Act.\(^\text{130}\) The


\(^{128}\) Equivalent to s CB1 of ITA 2004, s CD 3 of ITA 1994, s 67 (5) of ITA 1976 and s 88(a) of Land and Income Tax Act 1954.

\(^{129}\) Important to note interpretation of words “derived from any business”. This excludes capital Receipts eg CIR v City Motor Service Ltd [1969] NZLR 1010. In terms of derivation of income in the case of business income the most appropriate method is the accruals method of tax accounting. The *accruals* method treats income as having being earned when it is legally payable but not yet paid.
concept of a business is the exercise of an activity in an organised and coherent way to attain the end result of pecuniary profit. The word pecuniary was not defined in the earlier Acts. In Grieve, Richardson J noted: \(^{131}\) “... it simply reflects the underlying notion of income as being money or money’s worth. The profit sought must be in money or money’s worth and the business must be carried on for pecuniary profit.” There are no further statutory criteria set out in the Act to assist in identifying a business. This is basically a case law based rule.

The leading decision in New Zealand on the definition of a business is that of the Court of Appeal in Grieve v CIR. \(^{132}\) The taxpayer was a chartered accountant. He formed a partnership with his wife and entered into a written partnership deed. In the deed it was recorded that the partnership was carrying on the business of farming. The partnership showed recurrent losses from the year 1972 to 1977. The Commissioner disallowed 50% of the losses claimed for 1972 - 1975 and 100% for 1976 and 1977 on the basis there was no business being conducted. The issue before the Court of Appeal was to identify the correct approach to deciding what “business” was.

The Court of Appeal applied G v CIR\(^{133}\) and Richardson J sets out the test of what is a business. The test involves a two-step analysis: \(^{134}\)

(a) Nature of the activity

“Business” in the sense in which it is used in legislation conveys a notion of imposing a charge for tax in respect of revenue earning activities. The activity undertaken must be capable to being classified as a commercial or mercantile activity customarily engaged in as a means of livelihood and typically involving some independence of judgment and power of decision. It must be a pursuit or occupation demanding time and attention; a serious employment as distinct from a pastime.

130 Income Tax Act 2004 and prior Acts used the term pecuniary profit.


134 Grieve v CIR [1984] 1 NZLR 101, at p 110. The term business has broad application and any Activity meeting the two fold criteria would constitute business.
The activity was farming - and undertaken on a large scale - therefore it was commercial. Richardson J notes that:135 “The land area is sizeable and with appropriate development was close in terms of acreage to an economic unit capable of supporting a family and providing a suitable return on the investment from beef production.”

(b) Is the activity carried out with an intention to make profit?

Intention refers to the expectation that income will be derived. It is not the same as purpose which is the reason why the taxpayer does something. An expectation and willingness of profits to arise as a result of activity undertaken is material and not the purpose. Richardson J stated:136 “Some organised commercial operations may be embarked on without any motivation of profit-making and it is well settled that such activities may constitute trading.” In Grieve, Richardson J established that reasonable prospect of profit is not required to determine whether an activity is business or not. An actual intention once established is sufficient to establish whether business existed or not.

In G v CIR, McCarthy J stated137 that the essential test as to whether a business existed was the intention of the taxpayer as evidenced by his or her conduct and other factors such as recurrence were tests to ascertain the existence of that intention. He established the principles underlying the concept of profit making purpose or intention.138 McCarthy J noted:139 “I do not suggest that the appellant was motivated by the thought of the money which he expected to flow to him; I accept that his motives were of a higher order, but I think it would be unreal to believe that after some seven or eight years of this activity and these means of livelihood, he did not intend that his work should lead to gifts being made to him, gifts which he knew he would accept and use for his support. This, of course, was not the only purpose or

135 Grieve v CIR [1984] 1 NZLR 101, at p111.


intention of his activity; but intention to make a profit is commonly only one of the intentions of those in business”. The unsolicited donations received by the evangelist were held to be assessable. Californian Copper Syndicate derived a gain from the sale of copper producing land. The Court of Exchequer (Scotland) held that the gain was “a gain made in an operation of business in carrying out a scheme for profit making.”

In Grieve, Richardson J applied G v CIR and was of the opinion that the test of whether a business existed turned on the intention of the taxpayer as evidenced by his conduct. Conduct of the taxpayer is an objective test and the intent of the taxpayer is a subjective test, which is determined by examining external evidence apart from their stated intentions. In Grieve, Richardson J stated that a commitment to engage in business is not sufficient; rather a profit making structure must be established and ordinary current business operations begun. To decide whether the taxpayer has the necessary intention to make a profit factors to look at are: “Nature of the activity; statements of intent; period over which it is conducted; scale of operations and volume of transactions; the commitment of time, money and effort; the pattern of activity; financial results; comparison to similar activities.”

Nature of the activity - Real transactions
A business must involve real transactions and not just exist in the mind of the taxpayer. In Calkin v CIR the taxpayer paid to a Mrs P the sum of $167,500 which represented certain alleged purchases made by her of property of various kinds. The arrangement between them was that she would apply each sum received from the taxpayer to a particular purchase which she would sell promptly and profitably. The taxpayer would receive the proceeds less Mrs P’s commission. In fact Mrs P was engaged in fraudulent activities and subsequently she was convicted of obtaining charges under false pretences.

The key point was that in the view of the court the intended income earning activity

---

140 Californian Copper Syndicate (Limited and Reduced) v Harris (1904) 5 TC 159, at p 166.
143 Calkin v CIR (1984) 6 NZTC 61,781 (CA).
never commenced – there were no actual purchases or sales or any dealings with third parties. In *Grieve*, Richardson J observed: \(^{144}\) “A business cannot exist simply in the mind of the taxpayer. It involves real transactions carried on for pecuniary profit...”.

Recreational activities or hobbies are not businesses. \(^{145}\) An illegal activity can still be a business. \(^{146}\) The taxability of illegal profits relies upon the application of the ordinary concepts of income to the illicit activity, in short, ascertaining whether or not there is a business being undertaken. In *Partridge v Mallendaine*, \(^{147}\) one of the earliest cases to consider the taxability of illegal income, where the legislation was silent as to the legality or illegality of the activities, unlawful businesses were not to be given the advantage of being free from income tax.

*Statement of intent*

Once it is established that the real activity exists, intention with which the activity was undertaken must be determined. In *Grieve* the taxpayers in the partnership deed stated that they were in business. Referring to the relevance of statements by the taxpayer, a subjective test Richardson J noted: \(^{148}\) “Statements by the taxpayer as to his intentions are of course relevant but actions will often speak louder than words.”

*Period of time*

The period of time over which the income earning activity is carried on or repetition of activity shows that the taxpayer intends to carry out the activity with a profit making intention. However that fact alone is not conclusive.

\(^{144}\) *Grieve v CIR* [1984] 1 NZLR 101, at p 106.

\(^{145}\) *Case D54* (1980) 4 NZTC 60,825.

\(^{146}\) *Case D 57*(1987) 4 NZTC 60,852.

\(^{147}\) *Partridge v Mallendaine* (1886) 2 TC 179 at p 181, where Justice Denman said, “In my opinion if a man was to make a systematic business of receiving stolen goods, and to do nothing else, and he thereby systematically carried on a business and made a profit of £2,000 a year, the Income Tax Commissioners would be quite right in assessing him as if it were in fact his vocation. There is no limit as to its being a lawful vocation, nor do I think that the fact that it is unlawful can be set up in favour of these persons as against the rights of the revenue to have payment in respect of the profits that are made.”

\(^{148}\) *Grieve v CIR* [1984] 1 NZLR 101, at p 110.
An isolated transaction does not on its own prevent a finding that a business has been carried out. The whisky in *IRC v Fraser*\(^{149}\) is an example of this. The taxpayer, a woodcutter, bought through an agent a large quantity of whisky. The whisky was purchased with the sole object of resale at a profit. The taxpayer had no special knowledge of whisky, he did not take delivery of the whisky and the entire transaction was conducted through an agent. The whisky was sold at a substantial profit. Another famous example is *Rutledge v IR Commrs*,\(^{150}\) in which the taxpayer purchased and sold a million rolls of toilet paper – this was held to be a trade transaction.

However, generally there will be reasonable frequency of transactions and some continuity of effort.

*Scale of operations, volume of transactions*

When the activity is carried on on a large scale and carried on more frequently may be evidence that the taxpayer intends to carry out the activity with an intention of making a profit. The nature and quantity of certain subject matter may force the conclusion that the transaction is a trade transaction.

In *CIR v Stockwell*,\(^{151}\) the taxpayer had a full time job and devoted some spare time to share trading. Whether the taxpayer was carrying on share trading business in that situation required an analysis of the relevant facts and the taxpayer’s intention. The fact that the taxpayer believed the activity to be trade was of little assistance. Considering the degree of level of activity required for business to exist Hardie-Boys J observed that:\(^{152}\)

“one would normally expect to find a considerable number of purchases and sales over an appropriable period of time before he could be regarded as dealing in shares and a substantial capital investment before one would take the next step of regarding him as in the business of dealing shares.”

---

\(^{149}\) *IRC v Fraser* 24 TC 498. This case took place in 1942 but it does establish one important principal in relation to the existence of a business.

\(^{150}\) *Rutledge v IR Commrs* (1929) 14 TC 490.

\(^{151}\) *CIR v Stockwell* (1992)14 NZTC 9,190.

\(^{152}\) Ibid, at p 9,194.
However a person can undertake an activity in a small way and still be in business. In *Case G 17* the taxpayer had given up teaching in favour of growing flower plants. The court found that even though it was “only a small, fairly fragile concern” it was still operating as a business, trading for profit, as an operative coherent structure with clearly defined objectives, dependent on the taxpayer’s capital and work.

On the other hand the mere magnitude or extensiveness of the realisation of an asset does not of itself cause that realisation to become a business.

In *C of T v British Australian Wool Realisation Association*, the taxpayer association was formed for the purpose of disposing of wool stocks and reimbursing owners with the proceeds of the sale – in spite of the magnitude of the amount involved ($4.1 m) the Privy Council found that “merely realising assets is not trading”.

*Commitment of time, money and effort*

The commitment of time, money and effort by the taxpayer may be evidence that the taxpayer intends to carry out the activity with an intention of making a profit. In *Grieve*, the taxpayer committed substantial funds, and put in much effort and spent much time on their farm. This level of commitment was sufficient to support business intent.

*Pattern of activity*

When the activity is carried on in a systematic and organised manner, that may be evidence that the taxpayer intends to carry out the activity with an intention of making a profit. In *Grieve*, the development work was carried on in a systematic way. The organised programme meant the area of pasture land greatly increased. The farming operations followed a usual pattern. This was an important finding supporting business intent.

*Financial results*

Reasonable prospect of profit is not required to determine whether an activity is business or not. Although *Grieve* made losses Court recognised that this was a start.
up period and expenditures were high which did not preclude business intent.

**Comparison to similar activity**

When the activity is carried on in the same way as those which are the characteristic of ordinary trade that may be evidence that taxpayer intends to carry out the activity with an intention of making a profit. In *Grieve* the business operations were comparatively similar to farming operation. He kept proper accounts.

Considering the particular facts in a situation the intention test also determines when a business commences and terminates. In *Grieve*, Richardson J said that:155 “[b]usinesses do not cease to be businesses because they are carried out idiosyncratically or inefficiently or unprofitably or because the taxpayer derives personal satisfaction from the venture.”

The next part reviews a selection of the early leading cases dealing with gifts in the context of receipts from personal exertion and examines the application of the employment income (s CE 1), business income (s CB 1) and income according to ordinary concepts (s CA 1 (2)) criteria by the courts.

---

**Part 3**

**A Review and Analysis of the Cases**

3. **Categories of gifts**

---

To examine the application of the employment income (s CE 1), business income (s CB 1) and income according to ordinary concepts (s CA 1 (2)) criteria by the courts the leading cases which deal with receipts from personal exertion are summarised and chronologically reviewed as follows:

3.1 Gifts to employees
3.2 Gifts to independent contactors
3.3 Gifts to businesses

Some of the earlier leading cases in this area are English. Molloy cautions against relying on these cases too heavily.156 This is because the structure of the English Income Tax Act is different from the New Zealand Income Tax Act.157 He does however find these cases to be “helpful”158 but they cannot be relied on without taking this difference in to account. While both Australian and English cases are persuasive, Australian cases are likely to be more influential because the structure and wording of the Australian Act are closer to that of New Zealand.159 The fact that English schedules only referred to certain receipts meant that when the English courts were interpreting the Schedules they looked only to their words to determine assessability. It was not open to the courts to apply the economic concept.160 However, in New Zealand and Australia tax is levied on income and it was left to the courts to determine what income was.

3.1 Gifts to employees have been sub categorized as follows:
3.1.1 Gifts in general
3.1.2 Gifts made by employer to employee

157 The English Income Tax Act, since its inception two hundred years ago, has never contained a general definition of income and merely identifies certain receipts which have been singled out for taxation. The identification is done by way classification of receipts either by reference to certain types of receipt, for example interest, or by reference to certain specified sources, for example, employment or trade. There is no equivalent in United Kingdom Act to s CA 1(2) of the Act.
159 AP Molloy, Molloy on Income Tax, Butterworths, Wellington, 1976, at p 3.
160 Ryall v Hoare [1923] 2 KB 447, at p 454. Rowlatt J held that gifts were not taxable under Schedule D because they are not profits or gains at all.
3.1.3 Contractual receipts

3.1 Gifts in general

I. Seymour v Reed [1927] AC 554

Seymour a professional cricketer was employed on a salary by the Kent County Cricket Club, nearing retirement. His club, under its rules, granted him a benefit match. The granting of a benefit match was at the discretion of the club. The issue was whether £939.16s., the gate takings from the benefit match (which were eventually handed over to Seymour) was assessable to Seymour. The House of Lords found by a majority of four to one that the receipt was not assessable.

The judgment hinged around whether the receipt was a personal gift or received as part of Seymour's employment relationship. Viscount Cave LC said “if it is the latter, it is subject to tax; if the former it is not”.

161 He compared the gate takings to personal gifts made outside the gates by Seymour’s supporters. He said that there was no question that spontaneous gifts by members of the public were not gross income. Why should the gate takings, which were of the same nature, but given to Seymour by the club, be treated differently? He also said “If the benefit had taken place after Seymour’s retirement, no one would have sought to tax the proceeds as income: and the circumstance that it was given before but in contemplation of retirement does not alter its quality”.

162 Lord Phillimore distinguished earlier clergymen cases such as Blakiston v Cooper by pointing out that “some element of periodicity or recurrence ... makes another distinction between them and the cases of a single gift by an employee or employers”. He found the receipt to be a “plain gift not taxable as a profit or perquisite of employment”.

163 In summary the majority of the House of Lords found that the receipt was of the nature of a personal gift or testimonial rather than a result of the employment relationship.

161 Seymour v Reed [1927] AC 554, at p 559.

162 Seymour v Reed [1927] AC 554, at p 560.

163 Blakiston v Cooper (Surveyor of Taxes) [1909] AC 104.

164 Seymour v Reed [1927] AC 554, at p 570.

165 Seymour v Reed [1927] AC 554, at p 572.
Lord Atkinson in dissenting looked more closely at the question of whether substantially the receipt arose as a result of Seymour's employment by the cricket club. His Honour said “I cannot find anything in the case suggesting that the club, or its committee, had any motive, object or aim in giving the benefit of this match to Seymour, their officer, other than to reward him for the efficient discharge of the duties of his post”. He went on to say that if the match had not been a benefit match then the takings would have been gross income to the club. This contrasts with the quality argument given by Viscount Cave LC above. Viscount Cave LC felt that the receipt had the same quality as the donations made by the public whereas Lord Atkinson felt that the receipt had the same quality as other takings of the club. Lord Atkinson referred to the clergymen cases and said that “the test is whether from the standpoint of the person who receives the money it accrues to him by virtue of his office of employment”. Applying employment relationship test Lord Atkinson stated that Seymour received a claim to a benefit match in the discharge of his professional duties and was not a gift personal to him.

II. *Hayes v FCT* (1956) 96 CLR 47

Hayes, an accountant, was employed by Richardson who had a successful meat and small goods business. In 1944, on Hayes' advice, a company was formed to take over the business. Hayes owned about 2,500 out of 17,000 shares in the company, while Richardson chose not to have a controlling interest. The company did not prosper and in 1947 Richardson decided that he should resume control. He insisted that he own all the shares in the company and more or less forced Hayes to sell his shares to him. However, he did promise Hayes that “You won't lose anything; I will make it up some day”. Under Richardson's ownership the company did prosper once again and it was decided to form a public company. Richardson did very well out of this and received 212,000 shares in the new company on the sale of his original company. He felt that he had “done particularly well” and in a spirit of generosity gave shares to several people including 12,000 shares to Hayes.

---

166 *Seymour v Reed* [1927] AC 554, at p 563.

167 *Seymour v Reed* [1927] AC 554, at p 566.

168 *Hayes v FCT* (1956) 96 CLR 47, at p 49.

169 *Hayes v FCT* (1956) 96 CLR 47, at p 50.
Were the shares assessable income or a simple gift of property? It was decided by the High Court that the shares were a simple gift. Fullagar J had some useful comments to make in arriving at his decision. He said that:

“A voluntary payment of money or transfer of property by A to B is prima facie not income in B’s hands. If nothing more appears than that A gave to B some money ... or some shares then what B receives is capital and not income. But further facts may appear which show that, although the payment or transfer was a “gift” in the sense it was made without legal obligation, it was nevertheless so related to an employment by B of A, or to services rendered by B to A ... that it is, in substance and in reality, not a mere gift but the product of an income earning activity on the part of B and therefore to be regarded as income from B's personal exertion”.

Whether a receipt can be related to any income producing activity on the part of the recipient is decisive in determining the income character of the receipt. If it is impossible to relate the receipt to any income producing activity on the part of the recipient, it is a gain which is not earned but made by way of personal esteem or testimonial and therefore not assessable. Fullagar J looked firstly at the motive of the donor which he considered to be relevant but not decisive. He said that “the gift of the shares was motivated, at least to a substantial extent, by gratitude for services rendered, and advice and assistance given ... But gratitude for services rendered was by no means the sole or exclusive motive”. He found that Richardson and Hayes had a close personal relationship and Richardson discussed business matters with the taxpayer in an informal way. Richardson wanted to make it up to Hayes for forcing him to sell his shares.

What Fullagar J felt was decisive was a lack of “any employment or ‘personal exertion’ … which can be fairly said to have produced the receipt”. Hayes was only employed by Richardson from 1939 to 1944 and Fullagar J felt it would be absurd to

170 *Hayes v FCT* (1956) 96 CLR 47, at p 54.

171 *Hayes v FCT* (1956) 96 CLR 47, at p 56.

172 *Hayes v FCT* (1956) 96 CLR 47, at p 56  Fullagar J Stated: “What is decisive, in my opinion, is the fact that it is impossible to relate the receipt of the shares by Hayes to any income-producing activity on his part”.

47
suggest that the shares represented extra remuneration for that employment or from Hayes’ employment by the company from 1944 to 1950.

He also could not find that “the gift of the shares represented a reward or recompense for the general advice and guidance given informally on a number of occasions to Richardson personally ...”.173 Hayes was not employed to give advice such as this nor did he have a business giving such advice. The receipt of the shares was therefore found to be not assessable.

III. Wright v Boyce [1958]1 WLR 832 (CA)
In Wright v Boyce an impressive challenge to the decision, in Blakiston v Cooper (Surveyor of Taxes)174 was mounted by counsel for the taxpayer.

Mr Wright (the taxpayer), a huntsman, employed by the Master of the Hunt, received gifts at Christmas from followers of the hunt, supporters of the hunt and persons interested in the hunt. The payments were purely voluntary with no request being made for them. The donors were influenced to some extent by personal regard for the huntsman, who was a noted personality and gifts were informally collected at the meet on Boxing Day.

Counsel for the taxpayer sought to distinguish Blakiston v Cooper (Surveyor of Taxes) by arguing that there was a definite machinery of collection and organization which made it plain in what capacity the sum was received by the clergyman. He went on to point out that in this case there was no machinery or organization at all. He said that, in such a case as this, one must look and see why the payment was made because, until this was found out, it was impossible to answer the question whether it was received by the recipient in relation to his employment. In other words, counsel was trying to bring the case into line with Seymour v Reed 175 by arguing that the voluntary payments were made, not to the taxpayer in his capacity as the holder of the employment of huntsman, but to the man himself in recognition of his skill in carrying

173 Hayes v FCT (1956) 96 CLR 47, at p 57.
174 Blakiston v Cooper [1909] AC 104.
175 Seymour v Reed [1927] AC 554.
out his duties as huntsman. Counsel closed his submissions by arguing that each gift or payment must be considered individually as in many cases the giver was influenced by personal regard for the taxpayer and the way in which he performed his duties and it must be determined which were given in respect of the taxpayer’s employment and which were personal gifts.

The Court of Appeal approached this argument by holding that the payments were made in pursuance of a custom to make presents of cash at Christmas time to the person for the time being employed as huntsman. If the payments were made in pursuance of custom, then, prima facie, they were not payments to the taxpayer as an individual but payments, in accordance with custom, to the huntsman for the time being who happened to be the taxpayer. Accordingly, the Court found that the payments were made in respect of the taxpayer’s employment and received every yearly.

As regards Counsel’s submission that each payment should be considered individually, the Court accepted that the amount of any particular payment would vary according to the view taken by the contributor of the taxpayer, as huntsman and possibly as a man. Therefore, the Court held that this matter of personal regard went only to the quantum of the payment received and did not alter its character.

IV. Moore v Griffiths (Inspector of Taxes) [1972] 3 All ER 399
Moore was a professional football player who was employed by a football club. The club was a member of the Football Association and the taxpayer agreed under his contract to observe the rules of the association. Moore was chosen as captain of the England soccer team in the year it won the World Cup. After the cup had been won, the association announced that it had decided earlier that £22,000 should be paid to the members of the England team if they won the cup. The players decided that the £22,000 would be divided equally between the 22 players who formed the squad whether or not they had actually played. Thus Moore received £1,000. He also received from the manufacturers of a toilet preparation company £500 as “a prize” for being the best player in the World Cup championship together with an additional £250 for being the best England player. Brightman J in the Chancery Division found that the receipts were not gross income.
He began by considering the payment to Moore by the association, firstly discussing whether an employment relationship existed. He found that for practical purposes Moore had been in the employment of the association in relation to the World Cup but this relationship had “terminated before the taxpayer received or was aware of the possibility of receiving the ... bonus”.176 Was the payment for services rendered? “The payment had the quality of a testimonial or accolade rather than the quality of remuneration for services rendered.”177

Brightman J then considered whether the payment was gross income according to ordinary concepts. He set out the following factors, not in their order of importance:

(i) “The payment had no foreseeable element of recurrence.”178 He said that recurrence was not an essential element but it was relevant.

(ii) “There was no expectation of reward.”179 Moore was totally unaware that a payment might be made for winning.

(iii) The association had already dispensed with Moore's services when the payment was made.

(iv) One of the association's functions was to promote the sport of football and not to derive a benefit from the services of footballers. Therefore the award was to “mark its pride in a great achievement, not to remunerate ... the employee’s services”.180

(v) The payment to each member of the squad was the same even if he had not played at all. Therefore the payments were not “linked with the quantum of any services rendered”.181

Thus the payment from the association was found not assessable.

The payments from the toilet preparation company were held not to be assessable.

---


177 Ibid.

178 Ibid.

179 Ibid.

180 Ibid.

181 Ibid.
Moore did not know until after the championship that the company would be awarding prizes and he had never had any other dealings or connection with the company. The Court found that the prizes were plainly offered in order to publicise the company’s products. Moore performed no services whatsoever for the company. The company was wholly uninterested in any realistic sense, in the quality of the services performed by the taxpayer or by any other player. The payments were therefore not in the nature of reward for services rendered by the taxpayer to the football association, or to the club or, for that matter to anyone else. ¹⁸²

V. *Kelly v FCT* (1985) ATC 4283

Kelly was a student who played rugby league for a club in Perth. He did not have a written contract but received a set amount for each game played. He received a substantial cash award ($20,000) from a television station as a result of winning the West Australian National Football League's (WANFL's) Sandover medal. This medal was voted for by umpires and given to the best and fairest player of the season. It was held by Franklyn J (Supreme Court of Western Australia) that the cash award was assessable.

Franklyn J accepted that Kelly was not employed by the WANFL or the television company who gave the award. He said that Kelly was aware of the existence of the award but did not have any special hope of winning it. He discussed the aim of the TV company in giving the award. This was “to attract more viewers because of the financial award which the recipient would receive and to promote Channel 7’s image in the eyes of the viewing public”. ¹⁸³ Franklyn J said that “the donor's motive may in some cases be found to be relevant”¹⁸⁴ in deciding if a receipt is gross income “but it cannot be the determining factor”. ¹⁸⁵ He preferred to consider the quality of the receipt in the hands of the recipient. He found that Kelly was an employee of the club. Was there then sufficient nexus between Kelly's employment and the receiving of the award to characterise the receipt as gross income or alternatively was the payment in

¹⁸² Ibid.


¹⁸⁵ Ibid.
respect of services rendered? Franklyn J found that “it is quite clear that the $20,000 could not be said to be payment for services rendered”.\textsuperscript{186} He then considered if the award was related to Kelly's employment as a league player. He said that “it was a sum that he was eligible to receive by virtue of his employment if he could play well enough to secure the votes from umpires as fairest and best player”.\textsuperscript{187} “Here the payment is directly related to the performance by the recipient of his duty as an employee of the club”\textsuperscript{188} and therefore it is gross income. Because he had found the receipt to be gross income arising from Kelly's employment relationship he did not explore the possibility that it might be gross income according to ordinary concepts.

VI. Case V135 (1988) 88 ATC 855
The taxpayer was a senior member of the academic staff of an Australian university. She was obliged by her university, as a member of academic staff, to undertake substantial research. From 1 December 1983 to 30 September 1984 she was on Special Studies Program Leave from her university pursuing her research close to original sources not available in Australia. The Special Studies Program is a period of release from normal duties to engage in research or other scholarly work or to undertake a project related to teaching or to academic administration. At the same time she was the holder of a Commonwealth fellowship awarded by an overseas university. The fellowship provided meals and accommodation and an allowance of $1,562. While on Special Studies Program Leave the taxpayer was entitled to her usual salary in addition to the benefits under the fellowship.

At the Tribunal, Mr P.M Roach\textsuperscript{189} held that the fellowship allowance came to the taxpayer by way of gift and was not assessable income. It was held that although the fellowship was not unsolicited, the provision of the fellowship by the overseas university was gratuitous on its part and did not come to the taxpayer as a reward for any services rendered to the overseas university or to her home university. The Tribunal found that the fellowship benefit was conferred on the taxpayer by reason of her personal qualities as a scholar and her commitment to undertake the particular

\textsuperscript{186} \textit{Kelly v FCT} (1985) ATC 4,283, at p 4,287.

\textsuperscript{187} \textit{Kelly v FCT} (1985) ATC 4,283, at p 4,288.

\textsuperscript{188} \textit{Kelly v FCT} (1985) ATC 4,283, at p 4,289.

\textsuperscript{189} \textit{Case V135} (1988) 88 ATC 855, at p 860 (Mr P.M. Roach, Senior Member).
research.

**Theme**

A review and analysis of the ‘General Category’ cases reveals that where there is no contractual obligation for a payment to be made, and yet such payment is made based upon the personal attributes of the recipient rather than their employment status, such a payment is a mere gift.

In *Seymour, Case V135, Hayes* and *Moore* the payments were made as a mark of the donor’s regard, gratitude or esteem towards the recipient and were not related to the donee’s employment and as no services were rendered, these receipts were held as a mere gift. In *Moore* and *Hayes* payments were made after the employment relationship ended.

In *Moore* the court also considered whether the receipt was income according to ordinary concepts. It was found that there was no recurrence, regularity, no expectation of a reward, no contractual entitlement, no services rendered and therefore the receipt did not have an income character under s CA 1 (2) as well.

In *Hayes* there was only one payment, therefore whether the receipt was income according to ordinary concepts was not considered. However, a payment made due to the personal qualities and attributes of the recipient in relation to their employment is income in nature. In *Kelly* and *Wright* the payment was made due to the personal qualities and attributes of the recipient but there was a relationship between the gift received and taxpayer’s employment. Thus, the gifts were earned for being an employee and were held assessable under s CE 1.

### 3.1.2 Gifts made by employer to employee

**I. Laidler v Perry [1966] AC 16 (HL)**

Dr Laidler was a senior employee of a company. To maintain happiness amongst staff, every year at Christmas the company gave all employees (2,300), with a minimum of 10 year service, a voucher worth £10 which could be spent at the shop of employee’s choice. The voucher was given irrespective of the individual’s position in the company or length of service. The directors believed that the voucher helped to foster a spirit of
personal relationship between the management and the staff which was likely to be of advantage to the company.

Dr Laidler regarded the annual giving of vouchers as a pleasant Christmas gesture which he hoped would continue but which he did not expect as of right. In argument it was suggested that a payment of £10 as a payment for services would have been derisory, if not insulting, having regard to Dr Laidler’s high position in the company.

The House of Lords looked at the vouchers from the viewpoint of both Dr Laidler and the company. They found that although there were impulses of generosity and seasonal goodwill present, the directors were planning for good and future loyal service so that the company would prosper in the future. The vouchers were distributed by the employers in their capacity as employers and because they were employers with a view to obtaining beneficial results for the company in the future: they were received by employees in their capacity as employees and because they were employees. Accordingly, Lord Hodson having regard particularly to the regularity of the payments year after year and applying an exceptionality criterion held that the vouchers were not mere personal gifts, but emoluments received in the course of employment. Laidler’s assessment to income tax on the value of the voucher under the English equivalent of section CE 1 of the Act was upheld.

Lord Hodson suggested that when a payment is made by an employer to an employee the attitude of the employer making the payment may be just as relevant as the attitude of the employee who receives it. He stated:

“It is often said that payments such as these must be looked at from the standpoint of the recipients who treated them as Christmas presents. This is a useful guide in

\[190\] They were not gifts of an exceptional kind to meet exceptional circumstances and entirely unexpected.

\[191\] ITA 2007, s CE 1: “amounts derived by a person in connection with the employment or service of the person.”

\[192\] The English court hearing the original case was looking to see whether these were emoluments from employment and so forth rather than considering whether the benefit was income or not. The voucher or the gift comes from a company, there is no personal tie with the employee. A legal person cannot be “friends” with anyone and give them a goodwill gesture.

those cases where money is derived not from the employer direct but from outside source – I have in mind the Easter offerings of the parish priest in *Blakiston v Cooper*, but I should have thought that when the payment is made by the employer to the employee it is not irrelevant to look at the intention of the employer who pays the money”.

Where gratuitous payments are made by an employer to an employee, practical difficulties arise in deciding on which side of the line a particular gift falls. For example, a box of chocolates or a bottle of whisky or $5 at Christmas if everyone gets it, it is prima facie evidence that the recipients realise it is an incident of employment and thus income under ordinary concepts. The vouchers were paid to in relation to taxpayer’s employment, to induce employees to go on working well and employees expected them. It amounts, in effect, to a question of fact and degree. *Laidler* was such a border line case.

II. *Ball v Johnson* (1971) 47 TC 155

The taxpayer was a bank clerk. The staff handbook stated that each clerk “shall study and sit for” banker examinations. The policy existed because of advantages to the bank in having suitably qualified employees. The bank reimbursed part of candidate’s tuition fees and paid cash rewards to those who passed. Failure to sit exams did not disqualify a clerk from employment but passing assisted promotion. The taxpayer received cash rewards on passing exams and the amount was included in assessable income as the Commissioner considered the awards were remuneration for services with the bank. Plowman J held that receipts were not income from employment under the relevant English statutory schedule. The awards were given for the taxpayer’s personal success in the examinations and not as remuneration for his services with the bank. He found no relationship between the payment to a taxpayer and his employment.

The test in *Ball v Johnson* may be stated as follows: If a receipt is given to a person for his personal success and not for the services performed, then the receipt will not be gross income. The recipient is doing something to improve his human capital and he

---

194 *Blakiston v Cooper (Surveyor of Taxes)* [1909] AC 104.

195 Income Tax Act (1952) 15 &16 Geo. 6&1 Eliz.2.c.10 (United Kingdom), Schedule E.
receives a prize for doing so.

The approach of both the Australian and New Zealand tax acts allows a wider capture of employment related income.

**Theme**

A review and analysis of the ‘Employment’ cases where employers purport to make gifts to employees reveals that where a voluntary payment is made to an employee as a present or on grounds personal to that employee and is unrelated to their employment, such a payment is a mere gift.

In *Ball*, the employee was given a reward, not for acting as an employee but for his personal success in an examination. In this situation there was no relation between the particular benefit given to the employee and the employer. However, where such a payment *is* related to the recipient’s employment or service, it will be classified as income. In *Laider* employment was the direct cause of the payment. The scheme of giving away vouchers arose out of the circumstances of employment as they were ‘emoluments’ from employment. The vouchers were given to employees to motivate them for services rendered within their role as an employee.

3.1.3 **Contractual receipts**

I. *Blakiston v Cooper* (Surveyor of Taxes) [1909] AC 104

A published letter by the bishop of a diocese pointed out to parishioners that clergy were seldom paid sufficiently and requested that Easter collections should be devoted to the personal use of the clergyman of each parish. The bishop wrote that any amount given should donated “as a personal, non-official freewill gift”\(^\text{196}\) and that any offerings made would be given “on that understanding only”.\(^\text{197}\) Blakiston, the vicar of East Grinstead, received an Easter offering from the Easter collections.

The question was whether the amount received was assessable for income tax and the arguments centered on whether the amount was received as a result of the vicar's

\(^{196}\) *Blakiston v Cooper* (Surveyor of Taxes) [1909] AC 104, at p 105.

\(^{197}\) *Blakiston v Cooper* (Surveyor of Taxes) [1909] AC 104.
office (or employment relationship) or as a result of his personal qualities. The House of Lords decided that the receipt was assessable income.

Lord Chancellor said “in my opinion, where a sum of money is given to an incumbent substantially in respect of his services as incumbent, it accrues to him by reason of his office”. He went on to say that if the money had been “a gift of an exceptional kind” for example to provide for a holiday or a subscription peculiarly due to the personal qualities of a person then it would have been a personal present. He also said that although the persons concerned had done their best to make the receipt appear to be a mere gift, this was not its real character.

Lord Ashbourne said that the offerings were given as a result of a systematic appeal instigated by the bishop which related to all clergymen in his diocese, not just the vicar of East Grinstead. Therefore the offerings were made “for the vicar because he was the vicar”. It was pointed out by Lord Robertson that in writing the circular letter the bishop probably made it more likely that the receipt would be found to be assessable. The Easter collections were an annual event. This periodicity may have strengthened the case for treating the offering as gross income.

In *Blakiston v Cooper* the benefits were given for acting as an employee. The benefits arose out of the circumstances or incident of the office or employment, and were periodical, therefore held assessable.

II. *Mudd v Collins (HM Inspector of Taxes)* (1925) 9 TC 297

Mudd, a salaried accountant, the secretary and director of a company, negotiated the sale of a branch of company’s business. The company granted him £1,000 “as

---


201 Ibid.

202 *Graham v CIR* [1961] NZLR 994. The New Zealand court of Appeal decision in *G v CIR* deals with the question of whether an office holder is an employee. The court held that the minister was not an employee and s CA 1(2) was applied and he was caught under s CA 1 (2). Gifts given to the minister were found to be relevant product of taxpayer’s activities. However, the court treated him as been in business.
commission for his services in negotiating the sale”. Rowlatt J held that the payment of £1,000 was made in return for services rendered in relation to his employment. Mudd objected to the assessment of this payment to income tax on the grounds that the negotiation of the sale was not part of his duties as secretary and director. He argued that the payment was a voluntary gift which did not constitute a profit for income tax purposes. Rowlatt J rejected this argument and concluded:

“...it seems to me that [I]f an officer is willing to do something outside the duties of his office; to do more than he is called upon to do by the letter of his bond, and his employer gives him something in that respect, that is a profit, it becomes a profit of his office which is enlarged little so as to receive it.”

If an employee is willing to do something outside the duties of his office, and his employer gives him something in respect of this, it becomes a profit and is assessable as employment income.

Rowlatt J said:

“I ventured to throw out during the argument that there was a distinction between a testimonial and remuneration for services of this kind. When a man is given a testimonial because of his work in the past, not directly remunerating him for that work, but recognising how high a regard has been held for him in the association of people with him arising out of the performance of those services, and people recognise the good qualities he has and how zealous and kind he has been, and how eager to advance the interests of his employers or his parishioners or his constituents, or whoever they may be, and they say “We would like to give you something as a mark of our esteem and regard,” that is a testimonial.”

The test established by the court is that if the receipt is in return for services rendered beyond the scope of the duties, it is monetary remuneration and becomes assessable to income tax.

III. Louisson v Commissioner of Taxes [1942] GLR 477

In the Louisson case, voluntary payments were made by an employer to an employee who had enlisted or who had been called up for military service in order to make up

---
204 Mudd v Collins (HM Inspector of Taxes) (1925) 9 TC 297, at p 300.
their military pay to the amount of their wages. These payments were held, by the Court of Appeal to be personal gifts and not remuneration in respect of their employment or service with the company. In *Louisson v Commissioner of Taxes* case Myers CJ and Northcroft J commented as follows:

“It seems to us that in all cases where gratuities have been held to be assessable income there has either been service, or employment, or something in the nature of service or employment, as between the recipient and the donor. We cannot see that this can be said to be the case as between a member of the armed forces and an ordinary citizen even though the soldier may previous to his becoming a member of the armed forces have been in that citizens’ employment.”

Kennedy J said: “The Fact that the gift was made by making up the pay of the person who so enlisted to that which he had formerly received does not in my view make it any the less a gift not in respect of his employment. Nor does the fact that it was made to apply to all employees who enlisted seem to alter that conclusion. It was personal to each one …”.

In this case it was found that the extra pay was not gross income because the then equivalent of s CE1, s 88(1) (b) of the Land and Income Tax 1954, referred to an existing employment or service and cannot be treated as extending to an employment or service which has come to end. The court did not consider whether the extra pay was gross income according to ordinary concepts. Australian case *FCT v Dixon*, which has somewhat similar facts but in which the court came to a different decision, is discussed next. Like the *Dixon* case, if a New Zealand court would have considered s CA 1(2) of the Act, income according to ordinary concepts, then extra pay would have been income. The payments were regular periodical payments instead of a lump sum. The taxpayer depended on the payments to support himself and his dependents and they were paid for that purpose by the employer. They were substitute for salary and wages, that the taxpayer would have earned and paid if he would not have enlisted himself in the army. The payments were a gain derived in circumstances which give it in other respects an

---

205 *Louisson v Commissioner of Taxes* [1942] GLR 477, at p 481.


207 *FCT v Dixon* (1952) 5 AITR 443; 86 CLR 540.
IV. *FCT v Dixon* (1952) 5 AITR 443; 86 CLR 540

Dixon was employed as a clerk by a firm of shipping agents up to 12 July 1940. The firm had notified their staff in 1939 that if any staff members enlisted in the army, the firm would endeavour to make up their military pay to the same level as their civilian pay. Dixon voluntarily enlisted in the Australian army on 12 July 1940. His former employer, the firm of shipping agents, made up his pay to its former level. He was discharged from the army in 1945. He then returned to his job with the shipping agents although there was no obligation on either side for him to do this. The question to be decided by the court was whether the extra pay received by Dixon from his former employers was gross income. The High Court of Australia found by a majority of three to two that the extra pay was assessable as gross income according to ordinary concepts.

The arguments centered around whether the extra pay was gross income as a result of Dixon's employment relationship with the payer or whether it could be characterised as gross income according to ordinary concepts. The three judges (Fullagar J, Dixon CJ and Williams J) who found the extra pay to be gross income came to this decision through essentially the same pathways.

They found that they could not agree with the Commissioner that the extra pay was gross income because of Dixon's employment relationship with the shipping agents. Fullagar J said that “The fact of the respondent's employment explains the selection of him as a recipient, but in no degree characterises the payment”.208 He went on to say “The payment does not partake in any degree of the character of a reward for services rendered or to be rendered”.209 This was because the payment did not relate to Dixon's length of service nor the quality of his service as an employee of the shipping agents. Nor was there any obligation for him to return to their employment after the war. This argument was very similar to that used in an earlier New Zealand case with almost identical facts, *Louisson v Commissioner of Taxes*.210

---

208 *FCT v Dixon* (1952) 5 AITR 443, at p 453.

209 *FCT v Dixon* (1952) 5 AITR 443.

210 *Louisson v Commissioner of Taxes* [1942] GLR 477 (CA).
What distinguishes *Louisson* from *Dixon* is that in the latter case the court then went on to consider whether the extra pay was gross income according to ordinary concepts. The court considered other factors which give a receipt the quality of gross income. Fullagar J said that the receipts “were regular periodical payments - a matter which has been regarded in the cases as having some importance in determining whether particular receipts possess the character of income or capital in the hands of the recipient”.211 The existence of periodicity was found to be important but not decisive. What was found to be decisive was that the payments were a means of support for Dixon and his family and that the objective of making the payments was to add to the earnings, “the undoubted income”,212 of the recipient. Fullagar J said that:213

“What is paid is not salary or remuneration, and it is not paid in respect of or in relation to any employment of the recipient. But it is intended to be, and is, in fact, a substitute for ... the salary or wages which would have been earned and paid if the enlistment had not taken place. As such it must be income ... It acquires the character of that for which it was substituted and that to which it is added”.

The findings then of the majority of the court in *Dixon* were:214

• The payments could not be characterised as gross income because of the employment relationship which had existed between Dixon and shipping agents.

• No services were rendered by the recipient to the payer. Although this is a consideration in deciding whether a receipt is gross income according to ordinary concepts it is not an essential element.

• The receipt was found to be gross income because of the presence of other elements which indicate gross income according to ordinary concepts.

The fact that payments were regular and periodic in nature instead of being a single lump sum payment was significant. The taxpayer depended on the payments to support his dependents and him, and it was this purpose that the payments were made by the shipping

---

211 *FCT v Dixon* (1952) 5 AITR 443, at p 456.

212 Ibid Fullagar J.

213 Ibid.

214 Ibid.
agents. The payments were meant to act as a substitute for the salary and wages that the taxpayer would have earned had he not enlisted in the army. Therefore, the payments were a gain derived in circumstances which gave it an income character.

V.  Moorhouse (Inspector of Taxes) v Dooland [1955] 1 Ch 284

Dooland was a professional cricketer. Under his contract of employment he received a salary and other allowances but was also entitled to have collections on the field if he performed well. (There were strict guidelines as to when a player was entitled to a collection). During the 1951 season eleven collections were made for Dooland. It was held unanimously (though reluctantly) by the Court of Appeal that the income from the collections was assessable income.

Both Blakiston v Cooper\textsuperscript{215} and Seymour v Reed\textsuperscript{216} were considered at length. Both cases concerned the issue of whether voluntary payments by members of the public could be gross income as a result of an employment relationship. Sir Raymond Evershed MR said that “it has long been settled that payments voluntarily made by third parties to the holder of an office or employment may, in some circumstances, be taxable as profits arising to such holder therefrom ...”.\textsuperscript{217} Considerable care was taken to distinguish the facts in Seymour v Reed\textsuperscript{218} as on first reading they appeared to be similar. From his examination of the cases Sir Raymond Evershed MR deduced the following fundamental principles, which are worth quoting at length: \textsuperscript{219}

(i) “The test of liability to tax on a voluntary payment made to the holder of an office or employment is whether, from the standpoint of the person who receives it, it accrues to him by virtue of his office or employment, or in other words by way of remuneration for his services.

(ii) If the recipient's contract of employment entitles him to receive the voluntary payment ... that is a ground, and I should say a strong ground, for holding that, from the standpoint of the recipient, it does accrue to him by virtue of his

\textsuperscript{215} Blakiston v Cooper [1909] AC 104.

\textsuperscript{216} Seymour v Reed [1927] AC 554.

\textsuperscript{217} Moorhouse (Inspector of Taxes) v Dooland [1955] 1 Ch 284, at 301.

\textsuperscript{218} Seymour v Reed [1927] AC 554.

\textsuperscript{219} Moorhouse (Inspector of Taxes) v Dooland [1955] 1 Ch 284, at p 304.
employment, or in other words by way of remuneration for his services.

(iii) The fact that the voluntary payment is of a periodic or recurrent nature affords a further, but I should say less cogent, ground for the same conclusion.

(iv) On the other hand a voluntary payment may be made in circumstances which show that it is given by way of a present or testimonial on grounds personal to the recipient, as, for example .... a benefit held for a professional cricketer in recognition of his long and successful career ...”.

When these principles were applied to Dooland's situation, it was found that Dooland was entitled to the collections under his contract of service (and this was a right enforceable at law), which was not the case for Seymour. The collections had the same quality as other elements of Dooland's remuneration such as his salary although they may have been mere gifts on the part of the givers. Collections were made for Dooland eleven times during one season, whereas in Seymour's case only one benefit match was held near the end of his career. On these grounds the collections were found to be assessable income.

The statement of principle by Sir Raymond Evershed MR affirmed the decision in Seymour case. The judge went only so far as to draw together most of the diverse strands arising from earlier cases in order to formulate this broad set of principles. This statement of principle was cited with approval in Moore v Griffiths but it has never been universally adopted by the courts.

VI. Hochstrasser (Inspector of Taxes) v Mayes [1960] AC 376

Mayes was an employee of Imperial Chemical Industries Limited (ICI). He was required by the company to often move from one part of the country to the other. Under the company housing scheme the company agreed that it would make up any loss on the sale of a house by an employee when the employee was required to relocate. Mayes did make such a loss of £350 and it was reimbursed by the company. The House of Lords held unanimously that the reimbursement receipt was not gross

---

220 Moorhouse (Inspector of Taxes) v Dooland [1955] 1 Ch 284, at p 292 Evershed MR.

221 Moore v Griffiths (Inspector of Taxes) [1972] 3 All ER 399.

222 Refer to Laidler v Perry [1966] AC 16 at p 35. This case is discussed already in this paper at page 48 and Lord Hodson statement is cited there.
income.

The arguments centered on whether or not the receipt was a product of Mayes’ employment relationship with ICIL. Viscount Simonds quoted Parker LJ, who presided in the Court of Appeal hearing of the case, as follows:223

“Where you find that an employee has during the course of his employment received a benefit in money or money's worth, that receipt is a profit of his employment and taxable as such unless (1) it amounts to a gift to him in his personal capacity, eg., a benefit conferred out of affection or pity; or (2) it has been received for a consideration other than the giving of services”.

The receipt could not be characterised as a personal gift given out of affection or pity. In Hochstrasser v Mayes224 therefore the more important question was whether Mayes had provided services rendered in return for the receipt. The court found that Mayes’ salary was commensurate with others in similar positions and thus he was fully recompensed for the services he provided to the company. There was nothing express or implicit in the agreement to suggest that the payment was a reward for his services except the relationship of parties, which was not sufficient by itself to justify holding the payments assessable. As with other cases examined here, it was accepted that Mayes would not have received the money “but for” his employment relationship, but the “money was not paid to him as wages”225 and “it was not profits from his employment”.226 In Hochstrasser v Mayes227 it was held that the employment must be the causa causans of the payment and not merely the causa sine qua non. Lord Radcliffe expressed this principle by saying that while it is not sufficient to render a payment assessable that an employee would not have received it unless he had been an employee, it is assessable if it had been paid to him in return for acting as or being an employee.228

223 Hochstrasser (Inspector of Taxes) v Mayes [1960] AC 376, at p 388.
224 Hochstrasser (Inspector of Taxes) v Mayes [1960] AC 376.
226 Ibid.
228 Hochstrasser (Inspector of Taxes) v Mayes [1960] AC 376, at p 392.
The decision in *Pritchard v Arundale* affirmed the principles formulated in *Hochstrasser v Mayes*. In *Pritchard* the shares were given to Arundale under the tripartite agreement in consideration of his undertaking employment with the company and relinquishing his former career as a chartered accountant. The transfer of shares took place before Arundale started working for the company. It was held that the shares were not transferred “in respect of or in relation” to taxpayers employment in return for services. Consideration for the shares was the undertaking to serve the company.

VII. *Clayton (Inspector of Taxes) v Gothorp* [1971] 47 TC 168

The taxpayer was employed by a local authority. She was accepted by Bradford Institute of Technology (now Bradford University) for a nine month course which would enable her to be promoted. Before leaving the local authority she entered into an agreement with the council. The council lent her a sum equal to the salary she would have drawn if her employment had not ceased. She agreed to return and work for the Council for a period of not less than 18 months on completion of the course, at which time the loan would be cancelled. The loan was paid in monthly instalments during the course. The Inspector of Taxes assessed the taxpayer on the basis that the loan was an emolument of taxpayer’s employment.

Plowman J found that the consideration for the Council making the loan in the first instance was the taxpayer’s promise to do the course and then serve the Council for 18 months. This turned the loan into an absolute payment. It was thus a reward for past services and as such an emolument arising from the taxpayer’s employment. He concluded that the loan was assessable income as a reward for services, and it was immaterial that the right not to repay the loan stemmed from the loan agreement and not from the contract of service.

The distinction between *Pritchard v Arundale* and *Hochstrasser v Mayes* cases and *Clayton v Gothorp* case rests on the words “in respect of or in relation” to the taxpayer.

---

229 *Pritchard v Arundale* [1972] Ch 229.

230 *Hochstrasser (Inspector of Taxes) v Mayes* [1960] AC 376.

231 *Pritchard v Arundale* [1972] Ch 229, at p 306.
employment in return for services. In *Clayton* it was immaterial, in any realistic sense that the contractual receipt, the right not to repay the loan, stemmed from the agreement with the Council rather than the taxpayer’s contract of service. The payments to the taxpayer were found to be assessable because they related so closely to her employment that in fact arose from it. They were an emolument from her employment and so were caught by s 156(a) of the English Income Tax Act 1952 as amended (Schedule E).232

VIII. *FCT v Harris* (1980) ATC 4,238

Harris was employed by the ANZ Bank until November 1974. On retirement he became entitled to a pension under the bank’s staff pension scheme. In 1976 the bank made ex gratia unsolicited payments to most of the members of its pension scheme. The purpose of the payments was to offset the effects of inflation. The level of payment to each pensioner was not dependent on length or quality of service to the bank or the seniority of the pensioner prior to retirement. The question to be decided by the court was whether the lump sum payment was gross income or a gift. The Federal Court decided by a majority of two to one that the receipt was not gross income.

Bowen CJ reviewed the key elements which identify gross income under ordinary concepts. He said that “the first question which arises ... is whether the receipt was a product of (Harris's) employment with the Bank”.233 As with *FCT v Dixon*234 it was found that although Harris would not have received the payment if he had not been an employee of the bank “the receipt clearly was not the product of his employment in the sense of being produced by his service in that employment; the amount was in no way related to the length or quality of his service with the bank.”235

Other identifiers of gross income were considered. The question of periodicity was problematic. Only one payment was being considered by the court but it was

---

232 Income Tax Act (1952) 15 &16 Geo. 6&1 Eliz.2.c.10 (United Kingdom), “in respect of any office, employment or pension, the profits or gains arising or accruing from which...”.


234 *FCT v Dixon* (1952) 5 AITR 443.

acknowledged that Harris did receive further payments in subsequent years. Deane J (dissenting) found that the element of periodicity was present because of these subsequent payments. But Fisher J found that the receipt “was an unexpected and unsolicited lump sum payment”\textsuperscript{236} and there was no expectation that it would be repeated. \textit{FCT v Dixon}\textsuperscript{237} was referred to. In this case the payments were received weekly. Harris did not rely on the payment as a means of support. The quality of the receipt in the hands of the taxpayer was also considered. Reference was made to the dictum of Fullagar J in \textit{Dixon} in relation to a receipt: \textsuperscript{238} “it acquires the character of that for which it is substituted and that to which it is added”. In the case of Harris, the receipt was a supplement to Harris's pension which undoubtedly had the character of income. Again \textit{Dixon}\textsuperscript{239} was distinguished on the grounds that Dixon received a regular weekly supplement on which he could rely. Harris on the other hand received a lump sum payment with no assurance that he would receive another.

The majority of the Federal Court therefore found that the receipt was not gross income, it was unexpected and an unsolicited instalments of a fixed sum. It was not a substitute for salary and wages, that the taxpayer would have earned. The taxpayer was not depending on the payments to support himself and his dependents.

\textbf{IX. \textit{Naismith v CIR} (1981) 5 NZTC 61,046}

Naismith was the captain of a tug boat and was employed by the Northland Harbour Board. The tug boat rescued a vessel which had foundered off the Northland coast. The Board realised the vessel and its stores and subsequently distributed salvage moneys to the crew, including Naismith for performing services beyond contractual obligations. Thorp J at the High Court rejected the argument that the salvage money was a voluntary payment in the nature of a gift. The salvage money was paid in settlement of claims by the crew, it was received in relation to the taxpayer's employment and was for services rendered even though his entitlement to it arose

\textsuperscript{236} \textit{FCT v Harris} (1980) ATC 4,238, at p 4,247.

\textsuperscript{237} \textit{FCT v Dixon} (1952) 5 AITR 443.

\textsuperscript{238} Ibid, at p 456.

\textsuperscript{239} Ibid.
from the rules relating to salvage rather than the contract of employment itself. Therefore it was assessable. Thrope J said the receipt was caught by words “bonus, gratuity, or emolument of any kind…”

The presence of a direct employment relationship in deciding if receipts are income was important. Salvage money paid rested upon services rendered and services which gave rise to the claim for salvage were carried out during paid employment.

X. FCT v Blake (1984) 84 ATC 4,661 SC (Qld)
This case had very similar facts to FCT v Harris. The taxpayer was also a retired bank officer who received a voluntary supplement to his pension from the bank to cover cost of living increases. However the supplements were paid regularly along with the fortnightly pension. It was held by Carter J that the supplementary payments were ordinary income because it had been received over a long period of time, the taxpayer had a reasonable expectation that he would receive the supplement in the year in question, the supplement was used to meet the costs of living and was received with the regular pension which was income, the taxpayer only received the supplement because he had been in the employment of the bank and even though the payment of the supplement was voluntary, it was made out of genuine commercial considerations.

XI. Reid V CIR (1985) 7 NZTC 5,176
The taxpayer was enrolled in a primary teachers’ training course. He received student teacher allowance from the Wellington Education Board and undertook to teach for three years following the completion of the training course. The Wellington Education Board deducted PAYE from the allowance payments. The issue was whether the allowance was assessable to the taxpayer. The arguments centered on whether the amount was received as a result of taxpayer’s employment or service or in return for performance of the contractual obligations taken.

241 Ibid.
242 FCT v Harris (1980) ATC 4,238.
243 Ibid, the payments were unexpected.
Richardson J at the Court of Appeal accepted that there was no employment relationship between the taxpayer, a teacher’s training college student, and the Education Department. Thereby the allowance received was not assessable as an employment income. Then he considered whether the receipts were income according to ordinary concepts. He observed:\(^{244}\)

“If it has that quality of regularity or recurrence then the payments become part of the receipts upon which the recipient may depend for his living expenses, just as in the case of a salary or wage earner, annuitant or welfare beneficiary. But that in itself is not enough and consideration must be given to the relationship between payer and payee and to purpose of the payment, in order to determine the quality of the payment in the hands of the payee.”

The Court held that the receipts were in respect of and in return for Reid’s performance of the obligations which the taxpayer had taken by accepting the allowance therefore it constituted income according to ordinary concepts. Richardson J said “They were emoluments received in respect of and in return for his performance of the obligations of the studentship he had undertaken”.\(^{245}\)

He said that it is the character of receipts viewed from the taxpayer’s viewpoint that matters.\(^{246}\) There is no necessary connection between the character which a payment had in relation to the payer and its character as a receipt by the payee. To determine the quality of a receipt in the hands of the recipient consideration must be given to the relationship between the payer and the recipient and the purpose behind the payment. So long as the trainee teacher complied with his obligations he could expect the payments to continue.\(^{247}\) The payments were regular and periodic in nature instead of being a single lump sum payment was significant. The taxpayer depended on the payments to support his dependents and him, and it was this purpose that the payments were made by the Education Board. Therefore, the payments were a gain derived in circumstances which gave it an income character.

\(^{244}\) Reid v CIR (1985) 7 NZTC 5,176, at p 5,183.

\(^{245}\) Ibid.

\(^{246}\) Reid v CIR (1985) 7 NZTC 5176, at p 5184.

\(^{247}\) Reid v CIR (1983) 6 NZTC 61,624 Quilliam J.
However, the allowance was in the nature of a bursary and thus exempt income under s 61 (37) of the Income Tax 1976 (the then equivalent of s CW 36 of the Act).

XII. *Smith v FCT* (1987) 19 ATR 274

A bank had an “encouragement to study” scheme under which payments were made to employees who successfully completed approved courses of study. Smith was an employee of the bank who successfully completed an appropriate course and was accordingly awarded $570 by the bank. The High Court of Australia decided by a majority of three to two that the award was gross income.\(^{248}\)

This decision was based on the finding that there was sufficient nexus between the receipt and Smith's employment by the bank. Unlike *FCT v Dixon*,\(^ {249}\) Smith was still employed by the bank. Wilson J said that “the problem presented by the present case is whether the facts establish the requisite relationship between the benefit received by the appellant and his employment”.\(^ {250}\) He decided that there was no suggestion that the receipt was a personal gift. Instead “[t]he benefit is the product of a scheme embodied in the rules of the bank ... designed to not only encourage the efficiency of employees within it but to provide them with the incentive to advance their prospects of promotion ...”.\(^ {251}\) Brennan J said that “[e]mployment is more than the activity for which an employee is remunerated: employment comprehends all aspects of the relationship of employer and employee in the particular case save those aspects which are purely personal”.\(^ {252}\) He found that “[t]he scheme was an aspect of (Smith’s) employment. The allowance was not paid as a mark of an employer’s personal esteem for particular employees. I am quite unable to say that the allowance was paid for consideration extraneous to the employment”.\(^ {253}\) Thus the receipt was found to be assessable.\(^ {254}\)

---

\(^ {248}\) This case was actually heard by one judge in the NSW Supreme Court, three judges in the full Federal Court and five judges in the High Court of Australia. Of these nine, five judges found the receipt to be taxable and four found the receipt to be non-taxable.

\(^ {249}\) *FCT v Dixon* (1952) 5 AITR 443.

\(^ {250}\) *Smith v FCT* (1987) 19 ATR 274, at p 277.

\(^ {251}\) Ibid.

\(^ {252}\) *Smith v FCT* (1987) 19 ATR 274, at p 280.

XIII.  *Shell New Zealand Limited v CIR* (1994) 16 NZTC 11,303

Shell New Zealand Limited had a policy of making lump sum payments to employees who were transferred in the course of their employment. Each payment was made to compensate an employee for the loss incurred in having to change his or her residence. The lump sum was not calculated on the actual loss incurred but on the basis of two rather complex formulae relating to average house prices in different cities and whether the employee had a mortgage. Shell considered the payments to be reimbursements and therefore did not deduct PAYE from them. The Court of Appeal decided unanimously that the payments fell within the scope of monetary remuneration and were therefore subject to PAYE.

While distinguishing *Shell* from *Hochstrasser v Mayes*, the court identified two important distinctions. Firstly in *Hochstrasser v Mayes*, Mayes was compensated for the actual loss made, whereas Shell made lump sum payments based on two rather complex formulae. If Shell had compensated the actual losses, this would have added strength to the argument that the payments were simply reimbursements to employees. The court conceded that reimbursements for example of moving expenses are not taxable.

The second, and more important, distinction is that the wording of the New Zealand Income Tax Act is broader than the equivalent English section. The court in *Hochstrasser v Mayes* was unable to find that the compensation payment was captured by the words “in respect of any office, employment or pension, the profits or gains arising or accruing from which ...”. contained in the English Income Tax Act. Section CE 1 of the Act on the other hand uses the words: “Amounts derived in

254 See p 49 an earlier English case *Ball v Johnson* (1971) 47 TC 155, had an almost identical fact situation but the receipt was held not assessable. There was no contractual entitlement.

255 *Hochstrasser (Inspector of Taxes) v Mayes* [1960] AC 376.

256 Ibid.

257 Ibid.

258 Income Tax Act (1952) 15 &16 Geo. 6&1 Eliz.2.c.10 (United Kingdom) Schedule E.
connection with employment,” which offer a wider interpretation. The payments were made by Shell only because the employees were employees and required to move in the course of their employment. Mckay held that the payments were not salary or wages nor withholding payments but extra emoluments (of whatever kind), or other benefit in money. These facts were sufficient for s 65 (2) (b) of the Income Tax 1976 (the then equivalent of s CE 1of the Act) to apply.

Hence the presence of a direct employment relationship in deciding if receipts are income was important. The overall schemes under which the taxpayers obtained the benefits arose out of the circumstances of their employment and were in respect of or in relation to employment.

**Theme**

A review and analysis of the ‘Contractual Receipts’ cases reveals that where a payment is made to a recipient as a result of the recipient’s capacity as an employee and the benefit arose out of the circumstances of this employment or due to a contractual entitlement to the payment, such a payment is income in nature.

In Blakiston, Naismith, Mudd, and Smith the payments were made in respect of, or in relation to employment or service of the taxpayer. The benefit arose out of the circumstances of the employment and the payments were expected. In Smith the scheme was embodied in the rules of the bank. In Naismith services which gave rise to the claim for salvage were carried out during paid employment. In Blakiston a letter written by the Bishop clearly linked the receipt to Blakiston’s office of

---

259 ITA 2007.


261 Definition of emoluments is given in ITA 1976, s 2. ‘Extra emolument’, in relation to any person, means a payment in a lump sum (whether paid in one sum or in 2 or more instalments) made to that person in respect of or in relation to the employment of that person (whether for a period of time or not), being a payment which is not regularly included in salary or wages payable to that person for a pay period, but not being overtime pay: and includes any such payment made – “but does not include a payment of exempt income ...”.

262 Section 65(2)(b) states assessable income of a person is deemed to include, “All monetary remuneration.” The definition of monetary remuneration includes: “Any salary, wage, allowance, bonus, gratuity, extra salary, compensation for loss of office or employment, emolument (of whatever kind), or other benefit in money, in respect of or in relation to the employment or service of the taxpayer; and includes any expenditure on account of an employee [,but does not include any employer superannuation contribution].” Wording of UK Schedules was much narrower.
Clergyman. *Mudd* performed services beyond his contractual obligations. In *Hochstrasser* the United Kingdom Court held that the source of payment was a housing agreement and employment was not the cause of payment. The *Shell* case in New Zealand had somewhat similar facts but New Zealand Court did not follow that approach.

In *Shell, Dooland and Clayton* employment was shown to be the contributory cause of a benefit being paid. Taxpayer Dooland had a contractual entitlement to the payment. In *Clayton* and *Shell* the payments were emoluments arising from taxpayer’s employment. In *Dixon, Louissson, Blake* and *Harris* the payment was not made for being or acting as an employee, payments were made after the employment relationship ended. In *Reid* there was no employment relationship between the donor and the donee, however the payment was for future contractual obligation.

In *Dixon, Blake, Harris* and *Reid* the court considered whether a receipt was income according to ordinary concepts. In *Dixon, Blake* and *Reid* it was found that there was periodicity, recurrence or regularity, an expectation of reward and additionally the donee was reliant on the payments to support his dependents and himself, therefore the receipt had income character under s CA 1 (2).

However, where the recipient’s employment is not the cause of the payment and there is no contractual entitlement, the circumstances are exceptional, the payment is unexpected, and there is no regularity of payment, such a payment is a mere gift (Harris).

### 3.2 Gifts to independent contractors


In 1944 Mr G, a taxpayer, started working as an evangelist for the open Brethren Assemblies. There was no contractual relationship between the taxpayer and particular assembly. The general practice was to give gifts after a particular assembly had received a service from the taxpayer. The taxpayer also received gifts in the general course of his work. G had been preaching full time and receiving donations for 7 or 8 years prior to income years in question. The assessments under review were from 1953 to 1957. G supported himself and his family upon the donations he received.
from assemblies and individuals. This was the only means of financial support.

The Supreme Court was required to determine the assessability of gifts made to the taxpayer, an evangelist. The taxpayer contended that preaching was motivated by religious reasons and there was no profit making purpose or intent. McCarthy J stated that by 1953 the “pattern of [taxpayer’s] … income was well established.”263 The judge observed that when the taxpayer commenced preaching in 1944 he did not have an idea as to the level of contributions that will be given to him but by 1953 from his experience he knew and expected substantial contributions. McCarthy J held that gifts which were related to income producing activities of the taxpayer were assessable. The court recognised that higher principles motivated G in his preaching but considered that those gifts were received periodically with a profit making purpose or intent. Gifts were received by the taxpayer in anticipation that they will be a means of support for him and his family.264 The period over which the taxpayer carried out his activities was also key evidence that taxpayer was carrying on an activity with a profit making purpose or intent. The taxpayer’s intention as evidenced by his conduct shows that he was carrying on a business for pecuniary profit. He kept records of gifts received. Each gift was considered on its own facts. Only those gifts which were related to income producing activities of the taxpayer were assessable and mere personal gifts made purely as a mark of affection, esteem or respect were not.

Scott was a solicitor who had a long-standing client, Mrs Freestone. Among other things he acted for Mrs Freestone in connection with the realisation of some pieces of real estate left to her by her husband. Scott acted very assiduously on Mrs Freestone’s behalf and applied to have one piece of land rezoned. As a result the land was sold for a substantial profit. Mrs Freestone was very grateful for this and gave Scott a gift of £10,000. She also gave gifts to other people at the same time. The case was heard in the High Court before Windeyer J who found that the £10,000 was a gift and not assessable income.

264 Ibid.
The issue of whether Scott had been properly paid for services rendered as a solicitor was considered. Windeyer J,265 cited with approval a passage from the judgment of Kitto J in *Squatting Investments Co Ltd v FCT*,266 discussing the English case law, where his Honour said:267 “... The distinction those decisions have drawn between taxable and non-taxable gifts is the distinction between, on the one hand, gifts made in relation to some activity or occupation of the donee of an income-producing character ... and, on the other hand, gifts referable to the attitude of the donor personally to the donee personally.”

Windeyer J found Scott had submitted an account for his services and this had actually been paid after the gift was made.268 This pointed to the £10,000 being a gift “in the sense that it was gratuitous, not made in discharge of an obligation and not taken by the recipient as discharging an obligation”.269 The gift may have been given for faithful service but then so might for example a legacy. The presence of service does not of itself render a receipt income.270 Windeyer J could not find that the gift was captured by employment income. He then considered if it was income under ordinary concepts. He said “gifts of an exceptional kind, not such as are a common incident of a man's calling or occupation, do not normally form part of his income”.271 He went on to say that “[a]n unsolicited gift does not become part of the income of the recipient merely because generosity was inspired by goodwill and the goodwill can be traced to gratitude engendered by some service rendered”.272

265 Scott v FCT (1966) 117 CLR 514 at p 527-528.
266 *Squatting Investments Co Ltd v FCT* (1953) 10 ATD 126; (1953) 86 CLR 570. In *FCT v Squatting Investments Co Ltd* (1954) 88 CLR 413, Lord Porter held (at p 432) that an additional payment made voluntarily to the taxpayer was assessable because they supplied wool in the course of their trade. It was not a payment for personal qualities of the taxpayer but for goods and services supplied.
267 *Squatting Investments Co Ltd v FCT* (1953) 10 ATD 126, at p 149; (1953) 86 CLR 570, at p 633.
269 Ibid.
271 Scott v FCT [1967] ALR 561, at p 569. Windeyer J commented that a reward given by the owner of goods to the finder for his services is not assessable. It is extraordinary and there is no periodicity and no employment relationship.
This case was run as a test case by the Australian Tax Office (ATO) in order to clarify the assessability of receipts by athletes. Ms Joanna Stone had been a competitive javelin thrower since 1987. In 1991 she was employed as a senior constable in the Queensland Police Force, where she worked full-time until taking maternity leave in 2002. She was selected for the Queensland Academy of Sport in 1995, as a result of which she received benefits (cash and non cash). During 1996 she was selected for the Australian Olympic team in the 1996 Olympics in Atlanta. In the 1996 income year she was provided with a grant paid in monthly instalments by Athletics Australia and also received payment under the Medical Incentive Scheme. During the 1998 and 1999 income years also she received payments under this scheme.

In the 1999 tax year Ms Stone was selected as a member of Olympic Games “A” squad and during this year she participated in the Goodwill Games (in which she won prize money totalling US$ 6,000) and the World Cup (in which she won prize money totalling US $50,000). In her tax return for the 1999 income year, Ms Stone disclosed her taxable income of AU$39,832, which was her salary from Queensland Police Force. She also disclosed in her tax return that from her javelin activities she had received AU$136,448 which included the following categories of payment:

<table>
<thead>
<tr>
<th>Prize money at local and international sporting events</th>
<th>AU$93,429</th>
</tr>
</thead>
<tbody>
<tr>
<td>Government grants</td>
<td>AU$27,900</td>
</tr>
<tr>
<td>Appearance fees</td>
<td>AU$2,700</td>
</tr>
<tr>
<td>Sponsorships</td>
<td>AU$12,419</td>
</tr>
</tbody>
</table>

These amounts were not reported as assessable income and no claim was made for deductions relating to this activity. The Commissioner argued that these amounts were assessable. Ms Stone objected to this assessment by the Commissioner. At the Federal Court hearing Ms Stone agreed that the sponsorships amounts were assessable income and the Commissioner agreed that an award of AU$1,000 from Little Athletics payment was not assessable income. Hill J at the Federal Court held that Ms Stone’s activities went beyond the mere pursuit of a hobby to a level where Ms

---

Stone was carrying on a business (the business of being a professional athlete). All the rewards of that business were held to be incidental to that business and therefore income according to ordinary concepts. Hill J held that all receipts constituted assessable income except for the Queensland Academy of Sport (QAS) grant (AU$5,400) and the Oceania Amateur Athletics Association grant (AU$1,600) which were held not related to any service rendered by Ms Stone.

The High Court agreed with Hill J\(^{274}\) that Ms Stone was conducting a business as a professional sports person and she had turned her athletic talent to account for money.

The Court recognized the existence of sponsorship support was evidence that the athlete was a celebrity and/or a marketable activity. As Gleeson CJ, Gummow, Hayne and Heydon JJ stated:\(^{275}\)

“Once it is accepted, as the taxpayer did, that the sums paid by sponsors to her, in cash or kind, formed part of her assessable income, the conclusion that she had turned her sporting ability to account for money is inevitable. The sponsorship agreements cannot be put into a separate category marked “business”, with other receipts being put into a category marked “sport”. Nor can some receipts be distinguished from others on the basis that the activity producing a receipt was not an activity in the course of carrying on what otherwise was to be identified as a business”.

Four members of the Court (Gleeson CJ, Gummow, Hayne and Heydon JJ) said that:\(^{276}\)

“The payments were rewards from the conduct of business – the business of deriving financial reward from competing and winning in the athletics arena”.

While agreeing with the majority decision, Kirby J said that it was:\(^{277}\)

“… not necessarily a result to which I would have come, without the past authority accepted by this Court and uncontested in this case. In “ordinary concepts”, intermittent prize money and occasional special grants would not, in most Australian eyes (or in mine), be regarded as having the character of “income”, at least when such


receipts are viewed individually and in isolation from each other. Prizes, in particular, depend upon providence, are usually intermittent and ordinarily lack periodicity and regularity. They depend upon so many chance factors that they would not normally take on the character of “income” without some additional unifying ingredient.

It is the interposition of the postulate of the taxpayer's “business” that affords that additional ingredient that helps to link the several receipts and to colour them - each of them reinforcing the conclusion of the character of “income” that might not otherwise have been drawn reviewing them individually”.

The Court held that all of her income from sport was assessable, including the payment made by QAS (which had been treated by Hill J as non-assessable), and the payments made under the Medal Incentive Scheme on the basis that taxpayer was carrying on a business of being a professional athlete. The way she pursued the hobby may no longer be considered to be hobby by the ordinary person on the street.

Theme

A review and analysis of the ‘Independent Contractors' cases reveals that where a payment is made to a recipient as a result of the recipient’s capacity as an independent contractor, the benefit arose out of the circumstances of this contractual relationship and there was an expectation of a reward, such a payment is derived in the course of carrying on a business. Where a voluntary payment is made to a contractor in recognition of past services after the contractual relationship has ended such a payment is a mere gift.

In Stone and G, the taxpayers, while holding their office, carried out their activities with an expectation that they will be rewarded for their services. There was periodicity, recurrence or regularity in payments, an expectation of reward, they were reliant on the payments to support themselves and their dependents and they were keeping records of the receipts which established that they had a business.

In Scott the payments were made after the business connection had ceased and because there was no expectation of a reward. The amount was so much greater than Scott could have charged for services rendered that it had to be given “predominantly
in recognition of personal qualities” and therefore a windfall gain.

**3.3 Gifts to businesses**

I. *Californian Copper Syndicate (Limited and Reduced) v Harris* (1904) 5 TC 159.

*Californian Copper Syndicate* was incorporated on 5 February 1901. Its aim was to acquire copper and other minerals. Soon afterwards the company acquired copper bearing land for £24,000 and spent the remainder of its paid up capital in the development of the mine. The company never intended to, nor given its capital base, was financially capable of mining the minerals in the land. In April 1902 a parcel of land was sold with the balance being disposed of in August 1904, the consideration for the transactions being £300,000 in fully paid up shares in the purchaser company. Taxpayer claimed it had merely substituted one form of investment for another.

In its decision the court distinguished between an act done in what is truly the carrying on of a business and mere realisation of investment. Distinguishing between what is and is not business income Lord Justice Clerk and Lord Macdonald stated: “It is a quite well settled principle in dealing with questions of assessment of income tax, that where an owner of an ordinary investment chooses to realise it and obtains a greater price for it than he originally acquired it at, the enhanced price is not profit assessable to income tax. But it is equally well established that enhanced values obtained from the realization or conversion of securities may be so assessable, where what is done is not merely a realization or change of investment, but an act done in what is truely the carrying on, or carrying out, of a business …What is the line which separates the two classes of cases may be difficult to define, and each case must be considered accordingly to its facts; the question to be determined being - Is the sum or gain that has been made a mere enhancement of value by realizing a security, or is it a gain made in the operation of business in carrying out a scheme for profit-making?"\(^{278}\)

Lord Traynor in *Californian Copper Syndicate* observed that where what is done constitutes the carrying on or out of a business; profits from the realization of the asset may be assessable. He noted: “But it was said that the profit – if there was a profit –

\(^{278}\) *Californian Copper Syndicate v Harris* (1904) 5 TC 159, at p 165.
was not realised profit and therefore not taxable. I think profit was realized. A profit is realized when the seller gets the price he has bargained for. No doubt here the price took the form of fully paid up shares in another company, but if there can be no realized profit except when it is paid in cash, the shares were realizable and could have been turned into cash … I cannot think that income tax is due or not according to the manner in which the person making the profit pleases to deal with it”. 279

The court held that
-company was endeavoring to make a profit by a trade or a business.
-not a substitution of one form of investment for another.
-the fact that profit was taken in shares and not cash did not effect the position.
-company never intended to work the copper mine.
-purpose was to exploit the field by inducing others to purchase it.
-the turning to account of the investment was an essential feature of the company’s business.
-not a case of a company merely changing an investment of capital to pecuniary advantage.
-sale was a proper trading transaction.
-company formed to acquire the mineral fields, not to work them, but solely with the view and purpose of reselling them at a profit.
-the profit had been realized even though the price had taken the form of fully paid up shares in another company.

The Court of Exchequer (Scotland) confirmed that while the transaction was isolated one, land had been purchased not for mining but for sale and the profit made upon the sales were assessable to income tax.

At the outbreak of war in 1939, an agreement was made between the governments of the United Kingdom and Australia for the supply and purchase of all Australia’s surplus wool production for the duration of World War II, at a determined price. It was also agreed that the profits from any sale of such wool outside the United Kingdom would be divided equally between two governments. A Central Wool Committee was

279 California Copper Syndicate v Harris (1904) 5 TC 159, at p 167-168.
set up by the Wool Regulations to acquire wool and to distribute the payments from the United Kingdom to wool growers. It was also responsible for distributing any profits derived from the resale of wool.

At the end of the war a disposal plan was devised under which surplus stocks were to be transferred into the joint ownership of the two governments and profits will be shared equally. The Wool Realization Commission, the Australian subsidiary carried out the functions of Central Wool Committee. The wool Realization Act 1948 provided for distribution of profits to suppliers in proportion to the value of wool supplied. The taxpayer received the sum of £22,851 as its share of an interim distribution.

Their Lordships held that “the payment must be regarded as an additional payment voluntarily made to the respondents for wool supplied for appraisement”. The judgment was based on two factors. The first was that the taxpayer was in the business of supplying wool and the payment was made because they supplied participating wool in the course of their trade. Secondly there was a clear connection between the supply of wool from 1939-1946 and the payment was made in 1949. The discretionary act on the part of Parliament directly associated the payment with the wool supplied. The Act directed the payment to suppliers, and directed that the amounts payable should be in proportion to the amounts of wool growers supplied for appraisement. Therefore, the payments were assessable to income tax.

III. Walker v Carnaby Harrower, Barham & Pykett [1970] 1 All ER 502, 1 WLR 276

The taxpayers were a firm of chartered accountants. In their professional capacity they had been auditors to a large group of companies for many years. The parent company installed a centralised machine accounting and the services of the taxpayers were no longer required. In 1962, their contract to audit for the company was terminated. The company gave them £2567.5s, the equivalent of their fee for the last

---


282 This case was applied in Simpson (Inspector of Taxes) v John Reynolds & Co. (Insurances) Ltd [1974] 2 All ER 545 and approved by the Court of Appeal reported at [1975] 2 All ER 88.
year of office, as solatium for loss of the office as auditors. The cheque was unsolicited.

The Chancery Division found that a voluntary payment of this kind could not be treated as a receipt of a business which consisted of rendering professional services. The Court found the receipt to be a gift, in particular because the services rendered by the taxpayers had already been paid for.

The gift was not made as a consideration for services but by way of recognition of paid services or by way of consolation for the termination of a contract. It was held, therefore, not to be assessable to income tax. However, the New Zealand Legislature reacted to this by adding the words “compensation for loss of office or employment”283 to s 88(1)(b) to the Land and Income Tax Act 1954. This immediately clarified the law and removed all uncertainty by making compensation payments for loss of office assessable to income tax.


The taxpayer company carried on business as insurance brokers. They had for many years acted as adviser to C Ltd on all its insurance matters including pension schemes. In 1965 ICI Ltd acquired large shareholding in C Ltd and advised C Ltd to place all its insurances with another insurance company. Thereupon C Ltd informed the taxpayer company that its services would no longer be required. However, in recognition of the taxpayer’s company past services as insurance brokers C Ltd agreed to pay £1,000 per annum for a period of five years.

Russell LJ284 found that £1,000 received by the taxpayer was not a profit or gain arising or accruing to them from their trade of insurance broker. It was received after the business connection had ceased, therefore, was held as a wholly unexpected and unsolicited gift.


The taxpayer was a firm of estate agents who had put in a lot of work negotiating the purchase of a plot of land. They received a scale fee which was inadequate remuneration for the work done. Later on when this land was sold, the new owners had their own agents to carry out the development work of the land so the taxpayers were no retained. Although new owners had no legal obligation, they recognised that the taxpayers had done work which they were to benefit from and made an ex gratia payment. The receipt was held as assessable because it related to specific services which were inadequately remunerated and was expected by the recipient. Templeman J stated that [285] “in determining whether a gift is earned, and therefore taxable, or deserved and therefore not taxable the test seems to me to be to enquire whether the gift can be referred to the work of the recipient or whether it can be referred to the conduct of the recipient”.

VI. Federal Coke Co Pty Ltd v FCT [1977] 34 FLR 375; 77 ATC 4255
The taxpayer was a wholly-owned subsidiary of Bellambi, a coal mining company. In April 1970 Bellambi contracted to supply 350,000 tons of coke to Le Nickel, over a period of five years. In 1972 due to recession Le Nickel asked Bellambi to vary the terms of the contract from 350,000 tons to 132,000 tons. Le Nickel agreed to pay $1 million compensation to a wholly-owned subsidiary (Federal Coke) for the variation of a long term supply contract. The amount received by the taxpayer were not based on any estimate of the value of expected profits in the future to support conclusion that amounts were received as a compensation for loss of capital assets.

The subsidiary gave no consideration for the receipt and the receipt was not a product of any business or revenue producing activity carried by it. The taxpayer’s business was closed before Bellambi directed Le Nickel the manner payments to be made to Federal. Therefore the payment did not arise out of the functioning of taxpayer’s business when it was operating. Bellambi’s motive in directing the payment to subsidiary was to compensate the taxpayer for loss in the value of capital assets. It was held that the receipt was on capital account and not assessable in the

hands of the subsidiary. Bowen CJ said:286

“It does not appear to me that the motive of Bellambi of avoiding tax, whatever view one may take of that motive, when taken into consideration with all the circumstances of the case can alter the position so as to lead to a conclusion that the receipts in the hands of Federal bore the character of income and not of capital.”

Theme
A review and analysis of the ‘Business’ cases reveals that where a payment is made in the ordinary course of the business of the taxpayer or an ordinary incident of the business of the taxpayer, the taxpayer is carrying on a business in relation to that transaction and any income derived is assessable under s CB 1 of the Act. Where a voluntary payment is made to a business in recognition of past services after the business relationship has ended such a payment is a mere gift. However, if after closure of business, the payment is made to compensate for capital assets loss, it will be held to be a capital receipt and therefore not assessable.

_Californian Copper Syndicate_ was formed to acquire the mineral fields, not to work on them, but solely with the view and purpose of reselling them at a profit. It was a profit making scheme or undertaking by the company. The company was endeavoring to make profit by trade or business and the sale price being paid in the form of fully paid up shares in the purchaser company do not alter the nature of the transaction. In _Squatting Investment Co_ the discretionary payment was made in proportion to the wool supplied for appraisement in the course of their trade. Therefore the receipt was trade receipt.

In _McGowan v Brown and Cousins_ since the taxpayer’s were inadequately remunerated for their services, the gift was expected by them and hence the payment was derived in the course of carrying on a business.

In _Carnaby Harrower, Barham & Pykett_ and _John Reynolds & Co (Insurances) Ltd_ the payments were made after the business connection had ceased and because there was no expectation of a reward and the payments were not part of any

286 _Federal Coke Co Pty Ltd v FCT_ [1977] 34 FLR 375; 77 ATC 4255, at p 4265.
contractual agreement but in recognition of past services, therefore held as a mere gifts.

In Federal Coke Co the payments did not arise out of the functioning or circumstances of their business when they were operating. The payment was made after the closure of the business to compensate the taxpayer for the loss in the value of its capital assets and therefore was capital in nature.

The analysis of the leading cases demonstrates a flow in the legal concept of income and it has been constrained by judicial rules developed over time. Lehman and Coleman\(^{287}\) have argued that the view of Jordan CJ in Scott v C of T\(^{288}\) that ordinary concepts and common usage determine the parameters of income is no longer acceptable. They note that income is a concept shaped by the views of experts.\(^{289}\)

In the next part developing the conceptual framework I will attempt to arrive at certain tentative conclusions based upon established tax precedents.


\(^{288}\) Scott v Commissioner of Taxation (1935) 3 ATD 142 at 145; (1935) 35 SR (NSW) 215.

Part 4

The Conceptual Framework

4. Ways to Analyse Gifts from Personal Exertion Income

Continuing from the previous sections\(^\text{290}\) where I identified that there are two ways to analyse gifts from personal exertion income:

- Ordinary concepts (s CA 1(2)) includes employment income (s CE 1) and business income (s CB 1); or
- Ordinary concepts (s CA 1(2)), employment income (s CE 1) and business income (s CB 1) are disparate tests.

I will now attempt to arrive at certain tentative conclusions based upon established tax precedents. An appendix is attached at the end of part five which, in the form of a matrix, summarises the conclusions made in this part.

4.1 Section CE 1 Employment Income

How important is the existence of an employment relationship in deciding whether a receipt constitutes gross income? Under what circumstances might it be found that a receipt which results from the existence of an employment relationship is not gross income?

The difficulty arises in drawing a distinction between gifts which are additional remuneration and are therefore assessable as profits from employment and gifts which are purely personal, and have no relation to employment. From the cases reviewed the following general guideline can be derived: the greater the causal nexus between the receipt and the employment, the more likely that the receipt will be gross income. The following paragraphs amplify this guideline.

A critical element is the nature of the employment relationship: whether it is direct or indirect. The existence of a direct employment relationship with the donor strongly increases the likelihood of a receipt's being found to be gross income. In *Hochstrasser v Mayes* a direct employment relationship existed that is Mayes was employed by

\(^{290}\) Part 1 and Part 2 of this paper identifies the research question.
ICIL. The receipt was found not to be assessable but only because there was evidence that it was not a reward for services rendered. In *Smith* there was “a contemporaneous relation between the employment and the payment ...”. In other words Smith was still employed by the bank. This was a strong factor in finding the receipt to be gross income. In *Naismith v CIR* there was direct employment relationship. The key factor in finding the receipt of salvage money to be gross income was that the taxpayer performed services beyond his contractual obligations during paid employment. A direct employment relationship also existed in the *Shell, Clayton v Gothorp, Mudd v Collins* and *Laidler v Perry* and the receipts in question were found to be taxable.

If there is an indirect employment relationship and a sufficient nexus can be found between the receipt and the employment relationship then the receipt will be gross income. In most of the cases reviewed there was not a direct employment relationship with the donor. The receipts may have been donated by the public (*Blakiston v Cooper, Seymour v Reed, Moorhouse v Dooland, Wright v Boyce*) or by former employer (*Louisson, Dixon, Hayes, Harris, and Blake*). In some cases the donor was even more remote (*Moore v Griffiths, Kelly, Reid*). Often the court has found as in *Dixon* that “[t]he fact of the respondent’s employment explains the selection of him as a recipient, but in no degree characterises the payment.” This approach means that in many of the cases reviewed the receipt was found not to be gross income as a result of insufficient causal nexus between the receipt and the employment relationship. However, in *Blakiston v Cooper* the receipt was found to be gross income, partly because of the letter written by the bishop. The letter clearly linked the receipt to Blakiston’s office of clergyman that is there was sufficient nexus. In *Wright v Boyce* the payments were made in pursuance of custom every year which clearly linked the receipt to Wright’s office of huntsman that is there was sufficient nexus present. In *Moorhouse v Dooland* case Dooland’s contract entitled him to the collections so again

---


293 Earlier case such as *Barson v Airey* (1925) 10 TC 609 reinforce this point. In this case employees received bonuses for exceptional work. The taxpayers argued that the receipts were not in consideration for carrying out the work for which they were employed. But the nexus between the receipts and the employment was too close for the finding to be anything else but income. Such payments are clearly captured in New Zealand by the s CE1 of ITA 2007, amounts derived in connection with employment.

294 *FCT v Dixon* (1952) 5 AITR 443, at p 453.
sufficient nexus was present.

Seymour would not have received the benefit “but for” his employment relationship with the cricket club. Was *Seymour v Reed* therefore wrongly decided? Even though an employment relationship existed, the benefit received was found to be “a mere gift or present … made to (Seymour) on personal grounds and not by way of payment for his services”.295 It was a special mark of esteem for the career of the cricketer. A close reading of the cases shows that it is possible that, even if an employment relationship exists, a receipt which can be explained by this employment relationship may not be gross income. For the receipt to be gross income there must be, as discussed above, sufficient causal nexus between the receipt and employment. Receipt must be a product or consequence of employment and benefits must be received for being or acting as an employee. The nexus in *Seymour v Reed* is not as obvious as in *Moorhouse v Dooland* where there was an actual contract. But the rules of the club in *Seymour v Reed* allowed members to have a benefit match and Seymour knew of these rules and would surely have had the hope or expectation of being rewarded by a benefit match as long as he performed his duties well.296 If the match had been an ordinary match and not a benefit match, the gate takings would have been gross income to the club. The nexus is stronger than that present in *Kelly* where the $20,000 was given to Kelly by a television station. However, Kelly earned it because he performed his normal contractual duties so well over the season. In *Moore v Griffiths*, an English case, the receipt was found not to be gross income297 but the connection was more remote between the donor(s) and the employment than in *Seymour v Reed*. Other distinguishing factors were also present. Moore was not aware that the prize money was available when he played in the World Cup, and the money was given to all the players in the England squad, irrespective of whether they had actually played. The decision in *Case V 135* must be open to some doubt; as such receipt is likely to be an ordinary incident of an academic’s employment. It is submitted that if *Seymour v Reed* came before a court today the benefit receipt would be found to be gross income.298

---

295 *Seymour v Reed* [1927] AC 554, at p 559.

296 *Seymour v Reed* [1927] AC 554, at p 563 Atkinson LJ.

297 *Moore v Griffiths* [1972] 3All ER 399, at p 411.

If the receipt is a result of a systematic scheme under which payments are made to a group of recipients, not just the taxpayer, the receipt is more likely to be gross income. The converse also appears to be true: if a receipt is a result of personal qualities of the taxpayer it less likely to be gross income. In *Blakiston v Cooper* and *Smith* the payments were made to all persons of the same class as the recipients and were found to be gross income. The receipts were not personal testimonials as for example in *Seymour v Reed*. In cases such as *Hayes, Ball and Case V135* the receipts were personal gifts, and thus not part of any scheme.

Does the test in *Blakiston v Copper* represent an effective test for distinguishing between a mere gift and a gift made to reward services rendered? The test may be worded as: if a receipt is given to a person substantially by virtue of his office or employment, then the receipt will be gross income. In all the cases reviewed there was a direct or an indirect employment relationship. A line must be drawn between receipts which arise substantially by virtue of the employment and those which are either gifts given in a personal capacity or for which no services have been rendered. Ultimately the courts have to examine the facts in each case to see on which side of the line a receipt lies. In some of the cases the drawing of the line is very difficult. In *Seymour v Reed* and *Case V135* for example, the line was drawn on the side of the receipts not being gross income, although there was a reasonable nexus between the payments and Seymour's and the Australian’s academic employment. In *Kelly* on the other hand the line was drawn on the side of the receipt's being gross income although the connection was more remote.

A wedding gift is not assessable when given by an employer to an employee because “it amounts to a gift to (the employee) in his personal capacity ... a benefit

---

61, shows that there is a harder attitude today towards the realities of professional sport and what comprise the income of a professional sportsperson.


301 *Laider v Perry* [1965] Ch.192 (CA).

302 *Kelly v FCT* (1985) ATC 4283, at p 4286.
If a wedding gift is not assessable, what of an ex gratia payment to a successful athlete by his/her employer? In *Seymour v Reed* there was much discussion about whether the benefit was “a mere gift or present (such as a testimonial) ... made to (Seymour) on personal grounds” or whether it was assessable income. The judgments in other cases such as *Moorhouse v Dooland*, *Moore v Griffiths* and *Kelly* covered similar ground. What distinguishes these “sports” cases and the example of a gift given by an employer to a successful athlete is that in the “sports” cases the player performed their normal contractual duties well and earned their reward. What sometimes makes gifts taxable is that if the tie relates to the action of the player, for example, batting that triggered the gift. In *Moorhouse v Dooland*, Sir Raymond Evershed MR said:

“It follows, in my view that a gift or present made either upon some special occasion as a wedding, a century at cricket, a birthday or at a season of the year when it is customary to make presents, does not necessarily cease to be non-taxable merely because the ties that link the recipient and giver are or are substantially those of service and are not or not exclusively those of blood or friendship ...”.

In other words, the existence of an employment relationship does not mean that all receipts by the employee from the employer are gross income. In order for the gift to be taxable there must be either a reasonable nexus between the employment and the gift or it could be caught as gross income according to ordinary concepts (very unlikely if the payment was one off). Therefore it is submitted that the ex gratia payment would not be gross income.

---

303 *Hayes v FCT* (1956) 96 CLR 47, at p 57.

304 *Seymour v Reed* [1927] AC 554, at p 559.

305 *Moorhouse (Inspector of Taxes) v Dooland* [1955] 1 Ch 284, at p 304.

306 *Moore v Griffiths* [1972] 3 All ER 399, at p 411.

307 *Kelly v FCT* (1985) ATC 4283, at p 4286.

308 *Moorhouse (Inspector of Taxes) v Dooland* [1955] 1 Ch 284, at p 297.

309 *Herbert v McQuade* (1902) 4 TC 489. In *Herbert Collins* MR held (at p 500) that the test is whether from the standpoint of the person who receives it, it accrues to him in virtue of his office. It was held to be irrelevant whether the payment was voluntary or not.

310 *FCT v Rowe* (1995) 95 ATC 4691 where an ex gratia lump sum payment by the state government as
4.2 Section CB 1 Business Income

How important is the existence of a business relationship in deciding whether a receipt constitutes gross income? Under what circumstances might it be found that a receipt which results from the existence of business relationship, is not gross income?

The difficulty arises in drawing a distinction between gifts which are an ordinary incident of a taxpayer’s business and are therefore assessable as profits from business and gifts which are purely personal, and have no relation to a business. The following general guideline can be derived from the cases reviewed: The relationship between the payer and recipient and the purpose for the payment determines the character of the receipt. The following paragraphs amplify this guideline.

In G v CIR the receipts were the result of his ordinary activities of preaching the word of God, the very services he was supplying to support himself. The fact that his motive was not profit making was not relevant in deriving income. The taxpayer was carrying on an activity with a profit making purpose or intent and that was crucial to constitute a business.

In Stone a taxpayer received from her javelin activities prize money, government grants, appearance fees and sponsorships amounting to AU$136,448. Ms Stone had turned her athletic talent to earn money and that was held to be carrying on a business, since all the rewards of that business were held to be incidental to that business. The judges emphasised the importance of the “intention” of the taxpayer in relation to identifying a business objective and established the principles underlying the concept of intention from G v CIR. The Stone case shows that there is a harder attitude

reimbursement of costs incurred by a local government employee in connection with an inquiry into his performance was regarded by the majority as not assessable. It was not regarded as a reward for his services.

311 G[raham] v CIR [1961] NZLR 994, at p 1.000 McCarthy J: “I do not suggest that the appellant was motivated by the thought of the money which he expected to flow to him; I accept that his motives were of a higher order, but I think it would be unreal to believe that after some seven or eight years of this activity and these means of livelihood, he did not intend that his work should lead to gifts being made to him, gifts which he knew he would accept and use for his support. This, of course, was not the only purpose or intention of his activity; but intention to make a profit is commonly only one of the intentions of those in business”. The unsolicited donations received by an evangelist were held to be assessable.
today towards the realities of professional sport and what comprises the income of a professional sportsperson.

It is clear from *Californian Copper Syndicate* that an isolated or one-off transaction is capable of being a trading venture if the taxpayer entered into the transaction with the profit making purpose or intention. In *Squatting Investment Co*, the Australian Government did not have a legal obligation to make the payment to the farmers but they felt they had a moral obligation. The government passed the law enabling them to distribute the surplus to the farmers. The court held that payment was related to the amount of wool supplied and made in the course of their trade. It was a part of their income earning process and therefore the receipt was a trade receipt. In *McGowan v Brown and Cousins*, the taxpayer’s would not have received the payment “but for” being inadequately remunerated for the past services provided. The payment for past services provided was inadequate so the additional payment brought the taxpayers remuneration up to an adequate level. Therefore even though no business relationship existed at the time of payment, the receipt was part of the business or revenue-producing activity carried on by the taxpayers.

In *Scott* and *Walker v Carnaby Harrower* the receipts were personal gifts and not part of any scheme or part of their income earning process. In *Scott*, the defendant had been paid for his services as a solicitor.312 Similarly in *Walker v Carnaby Harrower* the firm of accountants had been paid for the annual audit. In *Simpson v John Reynolds*, also the taxpayer company had been paid properly for its services. In the *Carnaby Harrower Barham & Pykett, Scott* and *John Reynolds & Co* cases the amount was received after the business connection had ceased and therefore it was a gift in recognition of past services rendered to the client company over a long period. Ironically the size of the payment (£10,000) and no business relationship existing at that time in *Scott* probably increased the likelihood that it would be found to be a gift. The amount was so much greater than Scott could have charged for services rendered that it had to be given “predominantly in recognition of personal qualities.”313

---

312 *Scott v FCT* [1967] ALR 561, at p 567.

In Federal Coke Co the compensation payment was not a part of Federal Coke’s business or the carrying on of a revenue-producing activity. The wholly-owned subsidiary company gave no consideration for the payment made for variation of a long term supply contract and there was no business relationship between the parties. The receipt by a subsidiary was a compensation for loss of capital assets. If the compensation had been paid to the supplier, Bellambi itself, it will be treated as ordinary income in the course of carrying on the business.

The analysis shows that a gift is taxable when there is a reasonable nexus between the existence of business relationship and the gift. A gift is taxable under s CB 1 of the Act if received in the ordinary course of the taxpayer’s business or an ordinary incident of the business. A receipt in recognition of past services is a mere gift.

4.3 Section CA 1 (2) Services Rendered
How important is the existence of services rendered in deciding whether a receipt is gross income? Under what circumstances will a receipt be found to be gross income even if no services have been rendered?

The Australian Income Tax Assessment Act s 15(2) provides for the inclusion in a taxpayer’s assessable income of all allowances, gratuities, compensations, benefits, bonuses and premiums allowed, given or granted to the taxpayer which relate directly or indirectly to the taxpayer’s employment or to services rendered by the taxpayer. The New Zealand Income Tax Act includes “in connection with their employment or service” which is fairly close to services rendered. However in New Zealand the more likely approach would be to consider the presence of services rendered as an indicator of gross income according to ordinary concepts. This distinction is not crucial as either way the presence of services rendered increases the likelihood of a receipt being found to be gross income.

314 Australian Income Tax Assessment Act 1997, s 15(2): “in respect of, or for, or in relation directly or indirectly to any employment of or services rendered by him.”

315 ITA 2007, s CE 1.

316 Reid V CIR (1983) 6 NZTC 61,624 at p 61-627-61-628 Quilliam J commented that a person may give service without necessarily being in employment. But his judgment was not final.
decision in *Mudd v Collins* illustrates this principle. 

It is not necessary for services to be rendered for a receipt to be gross income as long as other factors which indicate gross income according to ordinary concepts are strongly present. In *Dixon* and *Louisson* the payments were periodic, were a means of support and were supplementing Dixon's army wages (which were clearly gross income). It was related to an income earning process. In *Harris*, Harris was not rendering any services to the bank in return for the supplement to his pension. Other factors which indicate gross income according to ordinary concepts were not strongly present. There was no real periodicity in the payments and Harris did not rely on the payments as a means of support. The receipt was a supplement to Harris’ pension, which clearly had the quality of gross income, but the presence of this factor was not enough to lead to a finding that the pension supplements were assessable. In *Hayes* also no services were rendered to his former employer. In *Ball* also, the payment was a mark of the personal success of the employee. In *Hochstrasser* a reimbursement amount was paid to the taxpayer in his personal capacity as a home owner.

The courts have distinguished between payments which can be said to have been earned by the recipient and are taxable, and those payments which have been deserved and are not taxable. A significant factor in determining whether a payment is related to the work or the conduct of the recipient is whether the gift was unexpected and unsolicited by its recipient. It would normally follow that if the gift does not relate to any particular work of the recipient then it has been deserved but not earned.

In a number of cases, courts have considered the factor of whether the recipient has been properly paid for the services rendered. If it is found that the recipient has been properly paid for services rendered then the receipt is less likely to be gross income. In *Hochstrasser v Mayes*, Mayes’ salary was commensurate with others in jobs similar to his. However, the author believes that this is true in almost every case. The gifts were made because of the way services were performed. A voluntary payment or gift that

317 *Mudd v Collins* (HM Inspector of Taxes) (1925) 9 TC 297, at p 300.

318 *Ball v Johnson* (1971) 47 TC 155.

319 *Ball v Johnson* (1971) 47 TC 155; *Hayes v FCT* (1956) 96 CLR 47.

320 *Ball v Johnson* (1971) 47 TC 155; *Moore v Griffiths* [1972] 3 All ER 399, at p 411; *Walker v
is not related in any way to personal exertion is not assessable. The work of the recipient is considered to be the activity upon which the tax is imposed but the conduct of the recipient is merely how the work is performed and is not the activity itself. In *McGowan v Brown and Cousins* taxpayer’s were inadequately remunerated for their services, therefore receipts from the new owners for those services were held as assessable.

Should the prizes received by a participant in quiz shows be assessed as gross income because services have been rendered?

An employment relationship would not exist between the contestant and the quiz show company. Therefore for the prizes to be assessed as income there would need to be strong factors indicating gross income according to ordinary concepts. A service rendered is one of these factors and it is hard to deny that the contestant is rendering services to the quiz show company. But if the Commissioner wished to assess these prizes he would need to show that (under the principles discussed so far):

- prizes were won often enough to be said to be periodic;
- the prizes were relied on as a means of support;
- the prizes had the same quality as other receipts which are gross income; and
  the intention of the quiz show company was that the prizes should be gross income.

It is unlikely that enough of these factors would be present with sufficient force for the prizes to be gross income. As for the one-off participant, it is extremely unlikely that any of the above factors would be present.

In the case of Olympic champions, it would be unrealistic nowadays to view these people as anything other than professionals. Any receipts connected with the performance of their sport are in the nature of gross income according to ordinary concepts and thus would be assessable. In *Stone* the taxpayer, Ms Stone agreed that

---


321 This approach is supported by the New Zealand Inland Revenue Department's publication *The Rule Book* (IR248) which outlines the tax requirements for all sportspeople (professional or amateur), who derive income from their sport. In line with *Seymour v Reed* however, sportspeople are advised
sponsorship payments were assessable on the basis that the sponsorship amounts were rewards for services rendered. In G v CIR the receipts were not the result of personal relationship but because of the services an evangelist was supplying. In Squatting Investment Co receipt was related to the amount of wool supplied in the course of their trade. In Californian Copper Syndicate the sale of a copper mine was a trade venture.

4.4 Section CA 1 (2) Periodicity, Recurrence or Regularity
How important is the existence of periodicity, recurrence, regularity\(^\text{322}\) in deciding if a receipt is income according to ordinary concepts? Under what circumstances might it be found that even if receipts are regularly received, the receipts are not gross income?

While the existence of periodicity is often cited as a sign of the presence of income, as submitted by Lehman and Coleman, “the recurrent nature of a receipt, where it is not an annuity, is a weak indicium of its income nature”.\(^\text{323}\) A payer may simply make a series of gifts to the recipient, “conferred out of affection or pity”.\(^\text{324}\) A mother for example may decide to give her son, a student, $50 a week to help support him. The decision in Louisson illustrates this principle. The court held that the supplements to Louisson's army wages were gifts given entirely voluntarily. A similar decision might have been reached in Dixon, but the court went on to consider whether other elements which indicated gross income, including periodicity, recurrence and regularity were also present. In Moorhouse v Dooland the fact that the collections were repeated was one element in finding they were gross income. Jenkins LJ for example said the “the fact that the voluntary payment is of a periodic or recurrent character affords a further, but I should say less cogent, ground ...”\(^\text{325}\) for finding that it is assessable. The

---

\(^{322}\) Parry v CIR (1984) 6 NZTC 61, 820 at p 61.824 Tompkins J stated that “regular” involves recurring at uniform or near uniform intervals. He further said: “[t] he Court must ... consider the number of transactions and the intervals of time between each thereby assessing the degree of uniformity or consistency of occurrence. In the end it will have to determine as a matter of fact and degree whether the events that occurred demonstrate a regular pattern of such transactions.”


\(^{324}\) Hochstrasser (Inspector of Taxes) v Mayes [1960] AC 376, at p 388.

\(^{325}\) Moorhouse (Inspector of Taxes) v Dooland [1955] 1 Ch 284, at p 304.
presence of periodicity in *Moorhouse v Dooland* was an important distinction from *Seymour v Reed*. In the *Moorhouse* case in distinguishing Mr Dooland’s circumstances from those of Mr Seymour, Sir Raymond Evershed MR at the Court of Appeal emphasized that, except in the rarest circumstances, Mr Seymour would have only one benefit towards the end of his professional career, and that the sum subscribed was very large compared with his regular salary. The court held that these factors were not present in *Dooland* and that the collections paid to him were properly treated as taxable income. However, the judge has no objective test to determine what is a large and a small subscription amount in relation to recipient’s regular salary. In *Moore v Griffith* and *Scott* lack of periodicity, recurrence and regularity in the payments lead to finding that the receipts were not income. In *Reid* the presence of periodicity, recurrence and regularity contributed to finding that the student teacher allowance was assessable. In *Harris* Bowen CJ said that “[t]he regularity and periodicity of the payment will be a relevant though generally not decisive consideration”.

In fact the element of recurrence in *Harris* was somewhat contrived given that Harris only received a few lump sum annual payments. In *Blake* periodicity was much more strongly present as Blake received the cost of living supplements fortnightly along with his pension. In *G v CIR* and *Stone* the presence of periodicity, recurrence and regularity contributed to finding that the particular activities were business.

The general consensus from the cases is that periodicity is an indicator of gross income according to ordinary concepts but is not an essential or even a strong element. Certainly in *Harris* its (somewhat weak) presence did not lead to a finding that the supplementary pension paid to Harris was assessable. Other factors indicating gross income according to ordinary concepts must be present in force as in *Dixon, Reid, Louisson, Blake, G v CIR* and *Stone*. Now in New Zealand under s CF 1(1) of the

---

326 Ibid.

327 *FCT v Harris* (1980) ATC 4,238, at p 4,240.

328 *FCT v Harris* (1980) ATC 4,238.

329 *FCT v Blake* (1984) ATC 4238. It is ironic that if it is shown that a taxpayer relies on a controversial receipt as a means of support it is more likely to be found to be income. This was certainly the case in *Blake* and *Dixon*. The effect is that better off taxpayers have less exposure to taxation.
Act\textsuperscript{330} and in Australia under s 27H of Income Tax Assessment Act 1936, a payment made to a taxpayer to supplement a superannuation pension is included in assessable income.

4.5 Section CA 1 (2) Expectation of Reward

How important is the idea of “expectation of reward” in deciding if an action can be characterised as “services rendered”? If a person performs an action unaware that another person intends to (or may) reward him/her for his/her action, can the action be characterised as “services rendered”?

Gifts are precarious in nature; their receipt is unexpected by the recipient. Since there is no legal obligation for the gifts to be made, they cannot be relied on with certainty. However, precarious income refers to earned income as opposed to unearned income\textsuperscript{331} and then although they are unexpected and uncertain, they are not regarded as being earned either, although they are often deserved.

In \textit{Laider v Perry}, in the context of a £10 gift voucher given to Dr Laider as a Christmas gift by his employer Lord Denning stated:\textsuperscript{332}

“[S] uppose it had been £100 a year which had been given to all the staff … at Christmas. In that case it would clearly be open to the commissioners to find that it was a reward, remuneration or a return for services rendered. But now suppose that, instead of £100 it was a box of chocolates or a bottle of whisky or £2, it might be merely a gesture of goodwill at Christmas without regard to services at all. So it is a question of degree. It seems to me that in this case when one finds that £10 a year was paid to each of the staff year after year, each of them must have come to expect the £10 as a regular payment, which went with their services. It was, I think, open to the commissioners to find that it was made in return for services. It is, therefore, taxable in the hands of the recipient.”

\begin{footnotesize}
\begin{enumerate}
\item Section CF 1(1) of the Income Tax Act 2007 provides that if the pension is payable regardless of whether the death or disability is attributable to service in one of the specified forces, and is in the nature of a normal service pension, it is assessable income.
\item \textit{Laider v Perry} [1965] Ch.192 (CA), at p 199.
\end{enumerate}
\end{footnotesize}
The idea of expectation of reward as an indicator of assessable income is discussed in *Moore v Griffiths*. Brightman J listed the factors which led him to the conclusion that the prize money received by Moore was not assessable. Included in this list was the fact that, “There was no expectation of reward. The taxpayer was totally unaware of the prospect of the payment prior to the services which he performed. The terms of his contract with his club did not contemplate that gratuitous payments of that or any type would be made.” In the *Case V135* the taxpayer was aware of fellowship awarded but no services were rendered for the fellowship. It was given on personal grounds. In *Ball*, Ball was unaware of any reward. Kelly in *Kelly v FCT* on the other hand did know of the existence of the award he eventually won and this knowledge counted against him. Similarly in *FCT v Dixon, Louisson v CIR* and *Reid V CIR* the taxpayers were aware of the receipts and receipts were relied upon as a means of support. In *G v CIR*, after every assembly Mr G expected substantial gifts or donations that he used to live on. The donations were associated with some income earning process and were earned income.

In *Scott*, Scott was unaware that Mrs Freestone had any intention of giving him a gift over and above the amounts he charged her for his professional services. This factor helped the court to decide that the gift was not assessable. Similarly in the *Walker v Carnaby Harrower Barham & Pykett* and *Simpson v John Reynolds & Co (Insurances) Ltd* cases the gift was unexpected, and therefore held as not assessable. In *McGowan v Brown and Cousins* since taxpayers were inadequately remunerated, the gift was expected by them, and they were not surprised to receive it. The taxpayers considered that while they had no legal right to the payment, they were morally entitled to it, therefore it was held to be assessable income.

In conclusion, if a taxpayer acts without expectation of reward this will be a strong factor in finding that a receipt is not gross income. The reward will be received without profit making purpose or intention and the taxpayer is not relying upon it to support himself and his dependents. Such payments are not earned but arise by virtue of luck and are made as a mark of personal esteem and testimonial. In *G v CIR*.

---

333 *Moore v Griffiths* [1972] 3 All ER 399, at p 411.

334 *G v CIR* [1961] NZLR 994, at 1,000 per McCarthy J: “I do not suggest that the appellant was motivated by the thought of the money which he expected to flow to him; I accept that his motives were of a higher order, but I think it would be unreal to believe that after some seven or eight years of
McCarthy J established the principles underlying the concept of profit making purpose or intention.

4.6 Section CA 1 (2) Intention of the Donor and Donee

How important is the intention of the donor in deciding if a receipt is gross income?

In some of the cases discussed in part 3 the donors clearly intended the payments to be gifts. In *Blakiston v Cooper* for example the bishop requested that the parishioners make personal, non-official freewill gifts to the clergy and no doubt the parishioners thought they were making gifts. We can assume in the two “cricket” cases that the fans intended that their donations to Seymour and Dooland were gifts for excellent play. In *Ball, Case V135, Scott* and *Hayes* the intention of the donors was quite clearly that the payments were personal gifts. In *Federal Coke Co* the intention of the donor was to compensate the taxpayer for loss in the value of capital assets. In *McGowan v Brown and Cousins* the intention of the donor was to compensate the taxpayer for underpayment for the work done and therefore held as assessable. On the other hand in *Hochstrasser* and *Shell*, the donors intended that the payments they made to employees to compensate them for the costs of moving were reimbursements. However in *Hochstrasser* the receipt was found not assessable because there was evidence that it was not a reward for services rendered.335 The source of payment was Housing agreement but actually it had no purpose other than to advance the interests of the employer.

In other cases the donors appear to be motivated by different forces. For example in *Dixon* the donor was probably motivated by patriotism. In *Harris* the motivation appears to be a paternalistic desire to assist former employees against the effects of inflation. In *Walker v Carnaby Harrower Barham & Pykett* and *Simpson v John Reynolds & Co Ltd* the gift was made as a consolation for the fact the services will no longer be performed by the taxpayer for the donor. In *Reid* the motive was clearly this activity and these means of livelihood, he did not intend that his work should lead to gifts being made to him, gifts which he knew he would accept and use for his support. This, of course, was not the only purpose or intention of his activity; but intention to make a profit is commonly only one of the intentions of those in business”. The unsolicited donations received by an evangelist were held to be assessable.

335 *Hochstrasser (Inspector of Taxes) v Mayes* [1960] AC 376, at p 392.
that the payment to Mr. Reid was for his day to day living expenses. It is submitted that while the motives of the donors in the cases reviewed are diverse and frequently not articulated there is no discernible relationship between these motives and the decisions reached by the courts as to the assessability of the payments. The motive of the recipient is not significant. In *G v CIR* the motive of Mr G was preaching and was not profit making but receipts were held as business income. It is the character of the receipt in the recipient’s hands that is significant; the motive of the donor is only significant so far as it bears, if at all on that character. In *Reid*, Richardson J stated: “It is accepted ... that the question as to the true character of the payment should be ascertained and judged in relation to the recipient rather than to the payer”. In *Californian Copper Syndicate*, the taxpayer entered into the transaction with the a profit making purpose or intention therefore it was deemed a trading venture. In *Squatting Investment Co* the receipt was a part of their income earning process and hence a trade receipt. In *Dixon, Louisson, Reid, Moorhouse, Blakiston, G and Stone* the donees received payments with a profit making purpose or intent, in an anticipation that they will be the means to support them and their dependents. It was this anticipation which gave the receipts the character of income.

### 4.7 Two Ways to Analyse Gifts from Personal Exertion Income

In *Dixon, Louisson, Reid, Blake, Moore, Ball, Hayes, Case V 135, Harris* and *Hochstrasser* payments were neither made to the recipient as an employee nor were they related to the recipient’s employment and thus held not assessable under s CE 1. However receipts by *Dixon, Reid, Blake* were held assessable under CA 1 (2). In *Louisson* the New Zealand court did not consider s CA 1(2) of the Act. Like the Australian case *FCT v Dixon, Louisson* has somewhat similar facts, if the New Zealand court would have considered s CA 1(2) of the Act, then extra pay would have been ‘income’. The presence of periodicity, recurrence and regularity was considered in *Moorhouse* and *Blakiston* but was not decisive. In *Ball, Hayes, Case V135, Seymour* and *Moore* payments were made based upon the personal attributes of the recipients and not their employment statuses. Since there was no profit making purpose or intent, payments were not regular and/or periodic, there was no expectation of reward, and

---

336 *Murray v Goodhews* [1978] 2 All ER 40, at p 46 per Buckley LJ.

337 *Reid v CIR* (1985) 7 NZTC 5,176, at p 5,184.
they were not derived in circumstances which gave them an income character under s CA 1 (2). In *Harris* there was no contractual entitlement, the circumstances were exceptional, it was unexpected, and no regularity or periodicity existed, and Harris was not depending on the payments to support himself and his dependents. Therefore the payment did not have an income character under s CA 1 (2). In *Shell*, the New Zealand Court of Appeal did not follow the Hochstrasser and held that the payment was related to the recipient’s employment under the then equivalent of s CE 1 of the Act.

In *Scott, Carnaby Harrower, John Reynolds & Co* and *Federal Coke Co* payments were not related to services provided or the recipient’s business activity and thus were not held assessable under s CB 1. The payments were made based upon the personal attributes of the recipient or to compensate them for loss of capital assets and not their business relations. Since there was no profit making purpose or intent, no services were provided, payments were not regular or periodic, and there was no expectation of reward, they were not derived in circumstances which gave them an income character under s CA 1 (2).

In all the cases reviewed, where gifts received by the taxpayer’s were held assessable under s CE 1, something that comes in or the payments were received something that comes in or with a profit making purpose or intent, in an anticipation that they will be the means to support them and their dependents, the payments were made by the donor for services rendered by the recipient and there was an expectation of reward to catch those receipts under s CA 1 (2). In *Shell, Naismith, Smith, Clayton, Mudd* the payments being instalments of a fixed sum were not periodical or recurrent. However, the general consensus from the cases is that periodicity is an indicator of gross income according to ordinary concepts but is not an essential or even a strong element.

In all the cases reviewed, where gifts received by the taxpayers were held

---

338 A payment in money, or a non-cash benefit, that is convertible into money. *Tenant v Smith* [1892] AC 150.

assessable under s CB 1, the payments were incoming, or the payments were received with a profit making purpose or intent (a trade venture), or in an anticipation that they will be the means to support them, the payments were made by the donor for services rendered or goods supplied by the recipient, and there was an expectation of reward. The factors capture those receipts under s CA 1 (2).

This analysis shows that the receipts which were assessed under s CE 1 and s CB 1 will also have a character of income according to the ordinary meaning of the word income under s CA 1(2). It is submitted that there is support from several important decisions for the first proposition. This result appears to be consistent with the relationship between s CA 1(2) and specific provisions s CE 1 and s CB 1 defining income. The default rule is that the various characteristics of income under s CA 1 (2) apply to all kinds of income. However in practice since under s CA 1(1) specific categories of income include employment income (s CE 1) and business income (s CB 1) if a receipt according to the true meaning of the word is not captured as income as a result of an employment relationship and business activity, then usually the courts will explore the possibility that the receipt may be gross income according to ordinary concepts. In Reid Richardson J said:340 “To come within the residual paragraph of s 65(2) (equivalent to s CA 1 (2) of the Act) the payments received must be income according to ordinary concepts and be derived from a source not otherwise covered in the earlier paragraphs of the subsection.” John Prebble suggested that there are gaps in the formal coverage of an income tax statute and that the statute needs a general, substance-over-form rule to protect the tax base.342 The manner in which s CA 1 (1) and s CA 1 (2) have been drafted suggests that when considering different sources of income, the drafters have given examples of income under s CA 1(1) and at the end they thought no omissions existed, so to cover any other income, they inserted s CA 1 (2) stating, that income can be according to ordinary concepts or according to the ordinary meaning of the word. In other words, it means that if there is no better

340 Reid v CIR (1985) 7 NZTC 5176, at p 5182.

341 Earlier paragraphs of the subsection include employment income and other specific provisions.

reason to give a technical meaning to a particular receipt, then we start off with the ordinary meaning of the word.
Tax law does not follow the economic definition and draw a distinction between income and gain.\footnote{W Chan, “Income – A subjective Concept”, (2001) Vol 7:1 New Zealand Journal of Taxation Law and Policy, p 26.} While the economist recognises all accretion to economic or spending power as income, tax law does not. The default rule in New Zealand is that gains are not taxable, for instance, gifts are not taxable in the hands of the recipient notwithstanding them representing a gain to that person.\footnote{Ibid.} However, gains that are income are specifically taxable under section CA 1(1) which includes s CB 1 and s CE1 and s CA 1 (2) of the Act.\footnote{Section CB 3 to CB 5 (sales from personal property) are not covered in this paper.} Many types of capital gains, which prima facie are not taxable, are being drawn into the tax base by virtue of particular legislative provisions.\footnote{Section CB 6 to s CB 23 of ITA 2007 contains series of provisions to catch land sales.} Nevertheless, the existence of the capital/revenue distinction in the Act is perhaps the most striking difference between the legal and economic concepts of income.

In an economic sense, the judicial criteria designed to distinguish gifts from payments for personal exertion are artificial. Under the economic concept of income, receipts constitute an increase in wealth regardless of their label, their source and the circumstances (ordinary or exceptional) under which they are given. Recurrence and expectation criteria reflect deviations from the economic concept of income.\footnote{C.C Plehn, “The concept of Income, as Recurrent, Consumable Receipts”, (1924) 14 The American Economic Review, March 1, p 9.} There are lots of rules in income tax law that relate to the definition of income that exist only for the purposes of income tax law. They do not reflect any other economic reality and have no other purpose.
Professor R Parsons\textsuperscript{348} further notes that a ticket received as a payment for services may be income, whereas a prize won by the ticket is something else. Under this thinking the winnings merely constitute the convertibility of income already derived into another form. There is no real dispute between economists and lawyers that gains which are a reward for personal exertion, from employment or from the rendering of services will be income.\textsuperscript{349}

The courts strive to maintain a balance between the Commissioner of Inland Revenue and the taxpayer as impartial interpreters of the Legislature’s intention. In each of the cases discussed in this paper, the courts have had to identify elements which could indicate gross income and then to decide whether the combined force of those elements are sufficient to say that a receipt is assessable. In many cases a unanimous decision has not been reached which indicates a significant level of subjectivity. The facts in \textit{Shell New Zealand}\textsuperscript{350} were somewhat similar to \textit{Hochstrasser}\textsuperscript{351} but the court came to a different decision finding that the reimbursement of moving costs was assessable in \textit{Shell New Zealand}\textsuperscript{352}. If the gift is no more than an independent voluntary gift made on purely personal ground, the payment or gift will not be assessable, regardless of the relationship between the donor and the taxpayer.\textsuperscript{353} Each case is very much decided on a close reading of the facts.\textsuperscript{354} In the ‘business receipts’ context, the judges attempt to distinguish between receipts from a taxpayer’s ordinary business operations and their capital gains from


\textsuperscript{350} \textit{Shell New Zealand Limited v Commissioner of Inland Revenue} (1994) 16 NZTC 11,303.

\textsuperscript{351} \textit{Hochstrasser v Mayes (Inspector of Taxes)} [1960] AC 376.

\textsuperscript{352} \textit{Shell New Zealand Limited v Commissioner of Inland Revenue} (1994) 16 NZTC 11,303.


\textsuperscript{354} Dooland for example was described by Birkett U as “a very fine cricketer” \textit{Moorhouse (Inspector of Taxes) v Dooland} [1955] Ch 284 (at p 308) and all the judges in this case expressed regret at having to find the collections to be gross income. Brightman J in \textit{Moore v Griffiths} [1972] 3 All ER 399 began his judgment (at p 403) with a comment that “In 1966 England won the World Cup for the first, but not, one hopes, the last time”.

106
investments.

A review of the case law shows that a recent number of leading cases in this area is not very large so it would be tempting to assume that the major issues have been dealt with. The Legislature, it is submitted, recognized the limitations of the sections which specifically make income from personal exertion assessable. To prevent the erosion of the tax base as discussed in 1968, Parliament introduced section 88 C\textsuperscript{355} in the New Zealand Land and Income Tax 1954. In 1973 section 88(1)(b) of New Zealand Land and Income Tax 1954\textsuperscript{356} was amended with the addition of “compensation for loss of office or employment as assessable income”. To overcome the deficiency in the legislation in making income from employment or services assessable, the New Zealand Income Tax Act 1994 was also amended in 2001.\textsuperscript{357} Certainly the definition of employment income in the New Zealand Income Tax Act 2007 is broad enough to capture most disputed receipts.\textsuperscript{358}

However, it could be that the expense of pursuing a case to court (as the majority of the taxpayers in this area are all individuals) mask any problems which could still be present. Certainly changes in the ways of working, for example the rise of professionalism in sport and the increase in consultancy and contractual obligation that does not arise from the employment could give rise to problematic issues in the

\textsuperscript{355} Section 88 C nullifies the decision in \textit{CIR v Parson} (No 2) [1968] NZLR 574, and overrides the old law by extending the meaning of “allowances” to include any benefit conferred on an employee under any share option or purchase scheme.

\textsuperscript{356} Section 88(1) (b) of the Land and Income Tax Act 1954 states assessable income includes: “all salaries, wages, or allowances (whether in cash or otherwise), including all sums received or receivable by way of bonus, gratuity, extra salary [compensation for loss of employment], or emolument of any kind, in respect of or in relation to the employment or service of the taxpayer.” This section along with s 88 C share purchase scheme, s 89 the provision of board lodging or housing by an employer, s 88 B retiring allowances by the employer is equivalent to s CE 1, of the Income Tax Act 2007. This amendment will alter the judgment for \textit{CIR v Fraser} (1996) 17 NZTC 12,607(CA).

\textsuperscript{357} New Zealand Income Tax Act 1994 was amended in 2001 to include restrictive covenants and exit inducement paid to employees or contactor as assessable income. Section CHA 1 and s CHA 2 were inserted in the Income Tax ACT 1994 with application to amounts derived on or after 27 March 2001. Section CHA 1 and s CHA 2 is equivalent to s CE 9 and s CE 10 of the Income Tax Act 2007. The payments to persuade staff to join (known colloquially as golden hellos) or to encourage bright staff to stay (golden handcuffs) are part of employment income and were assessable income as per Public Information Bulletin, No. 171, March1988 as well.

\textsuperscript{358} Section CF 1(1) of the Act now provides that if the pension is payable regardless of whether the death or disability is attributable to service in one of the specified forces, and is in the nature of a normal service pension, it remains assessable income. This means that in \textit{FCT v Harris} (1980) ATC 4238, the pension supplements now will be assessable.
In the present era universities are encouraging academic staff to opt for paid Special Studies Programs to undertake research relating to their specialised area. During that leave period, if the staff member, due to their personal qualities as a scholar receives fellowship allowance from the other university following the Australian precedent could New Zealand courts classify this as a gift? In author’s view employment is not the cause of the payment, the circumstances are exceptional, the payment is unexpected, and there is no regularity of payment therefore such a payment is a mere gift.

The effect of the changes in the 2007 Act is to remove a direct reference to “emoluments” which existed up until and including the 2004 Act. However, the author suspect that rather than being an attempt to change the law, the changes in the 2007 Act were intended to simplify the language of the source rules but retain the core concepts. The cross-reference to section CE 1 picks up concepts like allowance, bonus, extra pay, and gratuity, and perhaps it is considered these are wide enough to cover emolument. The author is unable to comment on whether in the future, while dealing with emolument payments, the courts will consider that the term “Extra pay” is essentially synonymous with the “emolument”. However, if this is so, it may explain why the drafters of the 2007 Act thought it was unnecessary in section YD 4(4) to specify an emolument. If emoluments are received in respect of or in relation to employment or being an employee they will be taxable under s CE 1or section CA 1(2) of the Act acts as a “catch all” provision, providing that amounts that were not specifically referred to in that legislation could still constitute income according to ordinary concepts and be taxed under Part C. The analysis from several important decisions also shows that there is a support for the first proposition that income according to ordinary concepts (s CA 1(2)) includes employment income (s CE 1) and business income (s CB 1). The analysis shows that the receipts which were assessed

359 In the case of Olympic champions, it would be unrealistic nowadays to view these people as anything other than professionals. The New Zealand Inland Revenue Department’s publication The Rule Book (IR248) outlines the tax requirements for all sportspeople (professional or amateur), who derive income from their sport. http://www.ird.govt.nz/forms-guides/keyword/individualincometax/ir248-guide-the-rule-book.html. Sportspeople are advised to seek advice if they receive any amounts from testimonials or benefits. The author hopes that the approach which is manifest in the majority decision of the High Court of Australia in Stone for determining what constitutes ordinary income will be followed by New Zealand courts while dealing with sports professionals and athletes.

under s CE 1 and s CB 1 will also have a character of income under s CA 1(2) of the Act which supplements specific provisions of the Act defining income. Sections CA 1(1) and CA 1(2) are not mutually exclusive and the author believes they were never intended to be. Section CA 1(2) is there to cover for any omissions and capture any forms of income which should be caught but are not included in the lists under Part C. Income according to ordinary concepts CA 1(2) acts as an umbrella provision and includes employment income (s CE 1) and business income (s CB 1). The manner in which legislation has been drafted shows that if there is no better reason to give a technical meaning to a particular receipt then we start off with the ordinary meaning of the word. Hence for receipts from personal exertion we tend first to look at the specific provisions under s CE 1 and s CB1 and only look later to see if a particular receipt comes within the ordinary meaning if it is not listed separately.

Therefore, the author believes New Zealand needs a conceptually sound Income Tax Legislation. The legal concept of income creates artificial distinctions about the nature of receipts and is based on the judicial interpretation and presence of selective criteria for a receipt or gain to be treated as income. The judicial concept of income is not compatible with the legal and economic concept of income. Often being subjective, judicial opinion inevitably varies, which undermines the objective of equity, neutrality and certainty in taxation. Kevin Holmes states that: “Unfortunately legislative reforms that have been designed to enlarge the legal concept of income have been piecemeal. Selected real economic gains have been grafted onto the traditional legal interpretation of income.”361

In author’s view, it is fair to conclude that for a neutral tax base the government should focus on the need for reform by enacting a legislation that embodies a provision specifically identifying income based on coherent income tax policy principles or objectives. The author believes that it will achieve greater horizontal equity, coherence, and theoretical robustness in tax system and Income Tax Legislation will be conceptually more sound and rational.

Appendix
Receipts from personal exertion
A matrix summarising the conclusions in part 4

<table>
<thead>
<tr>
<th>Factor</th>
<th>Assessable?</th>
<th>Cases which support the decision in column 2</th>
<th>Cases which refute the decision in column 2</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>ML = more likely</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>LL = less likely</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>N = neutral</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Direct employment relationship</td>
<td>ML</td>
<td>Smith Shell Naismith Clayton Mudd Wright</td>
<td>H v Mayes—even though Mayes was an employee the receipt was found to be not assessable</td>
</tr>
<tr>
<td>Indirect employment relationship</td>
<td>LL- but each case must be examined on its merits</td>
<td>Seymour Dixon Harris Hayes Louission</td>
<td>Blakiston Dooland Kelly Blake</td>
</tr>
<tr>
<td>Direct Business relationship</td>
<td>ML</td>
<td>Californian Copper Squatting Investment Brown and Cousins Stone</td>
<td>Walker John Reynolds Federal Coke Scott</td>
</tr>
<tr>
<td>Systematic scheme-payment to all people of same class</td>
<td>ML- but only just</td>
<td>Blakiston Dixon Smith Dooland Blake Wright Laider</td>
<td>Seymour Harris Moore</td>
</tr>
<tr>
<td>Personal one-off payment</td>
<td>LL</td>
<td>Scott Hayes Seymour</td>
<td>Kelly</td>
</tr>
<tr>
<td>Voluntary payment</td>
<td>LL</td>
<td>Ball Harris Hayes Federal Coke John Reynolds Walker v Carnaby Scott Moore</td>
<td>Kelly Mudd Brown and Cousins G v CIR Dooland</td>
</tr>
<tr>
<td>Relied on as a means of support</td>
<td>ML</td>
<td>Dixon Harris Blake Reid G v CIR</td>
<td>Louission</td>
</tr>
<tr>
<td>Factor</td>
<td>Assessable?</td>
<td>Cases which support the decision in column 2</td>
<td>Cases which refute the decision in column 2</td>
</tr>
<tr>
<td>--------------------------------------------</td>
<td>-------------</td>
<td>-----------------------------------------------</td>
<td>---------------------------------------------</td>
</tr>
<tr>
<td>Presence of services rendered</td>
<td>ML</td>
<td>*H v Mayes</td>
<td>*Smith</td>
</tr>
<tr>
<td></td>
<td></td>
<td>*Harris</td>
<td>Dixon- no services rendered but still found</td>
</tr>
<tr>
<td></td>
<td></td>
<td>*Scott</td>
<td>to be assessable</td>
</tr>
<tr>
<td></td>
<td></td>
<td>*Walker and Carnaby</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>*John Reynolds</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>*Hayes</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>*Case V 5</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>*Ball</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>*Louisson</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>*In these cases no services were shown to be</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>rendered, therefore not assessable</td>
<td></td>
</tr>
<tr>
<td>Periodicity</td>
<td>ML- but a weak indicium</td>
<td>Dixon</td>
<td>Louisson</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Reid</td>
<td>Harris- periodicity was present but not</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Dooland</td>
<td>assessable</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Blakiston</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>G v CIR</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Blake</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Reid</td>
<td></td>
</tr>
<tr>
<td>Payee has an expectation of reward</td>
<td>ML</td>
<td>Dixon</td>
<td>Harris</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Dooland</td>
<td>G v CIR</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Moore</td>
<td>Squatting Investment</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Kelly</td>
<td>Californian Copper</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Smith</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Blake</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Reid</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Brown and Cousins</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Stone</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>G v CIR</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Squatting Investment</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Californian Copper</td>
<td></td>
</tr>
<tr>
<td>Same quality as other receipts which are</td>
<td>ML</td>
<td>Dixon</td>
<td>Harris</td>
</tr>
<tr>
<td>gross income</td>
<td></td>
<td>Brown and Cousins</td>
<td>Ball</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Blake</td>
<td>Seymour</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Reid</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>G v CIR</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Californian Copper</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Squatting Investment</td>
<td></td>
</tr>
<tr>
<td>Intention of donor and done that the</td>
<td>Neutral- not a very relevant factor</td>
<td></td>
<td></td>
</tr>
<tr>
<td>receipt is not gross income</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

111
References

Bibliography


**Inland Revenue Department publications**


*Payments and gifts in the Maori community*, 1998, April 25, Wellington, IR 278.

*Public Information Bulletin*, Inducement Payments — Also known as “Golden Hellos” and “Golden Handcuffs” Number 171, March 1988.


*The Rule Book* (IR248) outlines the tax requirements for all sportspeople (professional or amateur), who derive income from their sport.

**Cases**


*Arthur Murray (NSW) Pty Ltd v FCT* (1965) 114 CLR 314.

*BP Australia Ltd v FC of T* [1965] 3 All ER 209.

*Ball v Johnson* (1971) 47 TC 155.

*Ball v Johnson* (1971) 47 TC 155.

*Barson v Airey* (1925) 10 TC 609.

*Birkdale Service Station Ltd v CIR* [2001] 1 NZLR 293; (2000) 19 NZTC 15,981.

*Blakiston v Cooper* [1909] AC 104.

*Brent v FCT* (1971) 125 CLR 418.


*Bryson v Three Foot Six Ltd* [2003]1 ERNZ 581; [2005] NZSC 34.

*California Copper Syndicate v Harris* (1904) 5 TC 159.


*Case D 14 (1979)* 4 NZTC 60,507.
Case D 54 (1980) 4 NZTC 60,825.
Case D 57 (1987) 4 NZTC 60,852.
Case G 17 (1985) 7 NZTC 1,065.
CIR v Fraser (1996) 17 NZTC 12,607 (CA).
CIR v Stockwell (1992) 14 NZTC 9,190.
C of T v British Australian Wool Realisation Association [1931] AC 224.
Constable v FCT (1952) 86 CLR. 402.
Cunningham v TNT ExpressWorldwide (NZ) Ltd [1993] 1 ERNZ 695.
Curlew v Harvey Norman Stores (NZ) Pty Ltd [2000] 1 ERNZ 114.
Ducker v Rees Roturbo Development Syndicate Ltd. (1928) A.C. 132.
Eisner v Macomber (1919) 252 US 189.
FCT v Blake (1984) 84 ATC 4,661 SC (Qld).
FCT v Dixon (1952) 5 AITR 443.
FCT v Harris (1980) ATC 4238.
FCT v The Myer Emporium Ltd 87 ATC 4,363.
FCT v Squatting Investment Co Ltd (1953) 86 CLR 570.
Federal Coke Co Pty Ltd v FCT [1977] 34 FLR 375; 77 ATC 4255.
Hayes v FCT (1956) 96 CLR 47.
Hochstrasser (Inspector of Taxes) v Mayes [1960] AC 376.
Hobbs, v. Hussey (1942) 1 KB 491.
IRC v Fraser 24 TC 498.
Kelly v FCT (1985) ATC 4283.
London County Council v A-G [1901] 4 TC 293.
Mangin v CIR [1971] NZLR 591 (PC) and CIR v Alcan NZ Ltd (1994) 16 NZTC 11,175.
McGowan (Inspector of Taxes) v Brown and Cousins [1977] 3 All ER 844.
Moore v Griffiths (Inspector of Taxes) [1972] 3 All ER 399.
Moorhouse v Dooland [1955] 1 Ch 284.
Mudd v Collins (HM Inspector of Taxes) (1925) 9 TC 297.
Pritchard v Arundale [1972] Ch 229.
Partridge v Mallendaine (1886) 2 TC 179.
Reid v C of R (1985) 7 NZTC 5,176.
Rutledge v IR Commrs (1929) 14 TC 490.
Ryall v Hoare (1923) 8 TC 521.
Seymour v Reed [1927] AC 554.
Shell New Zealand Limited v CIR (1994) 16 NZTC 11,303.
Smith v FCT (1987) 19 ATR 274.
Squatting Investments Co Ltd v FCT (1953) 10 ATD 126; (1953) 86 CLR 570.
Tenant v Smith [1892] AC 150.
Wright v Boyce [1958] 1 WLR 832 (CA).

Statutory References

New Zealand
Estate and Gift Duties Act 1968.
The Employment Relations Act 2000.
Land and Income Tax Amendment Act(No. 2) 1968.

Australia
Australian Income Tax Assessment Act 1936.
Australian Income Tax Assessment Act 1997 (Cwlth).

Great Britain

Income Tax Act (1952) 15 &16 Geo. 6&1 Eliz.2,c.10 (United Kingdom).