

# THE *PETERSON* CASE AND ITS IMPACT ON THE RULES IN *BEN NEVIS*

James Coleman\*

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*This article revisits and builds upon Professor Prebble's 2006 book chapter "The Peterson Case and its Impact on the Rules in BNZ Investments Ltd and Cecil Bros", considering the ways in which the Peterson case has influenced the leading 2009 New Zealand tax avoidance case of Ben Nevis. The article argues that Ben Nevis actually follows Peterson in two ways. First, it adopts the analysis of both the majority and the minority judgments in Peterson to the effect that the general anti-avoidance provision only applies when the purpose of the particular provision has been thwarted. Secondly, it uses the minority's less judicial approach in considering whether the purpose of the specific provision has been complied with or not. The minority allowed a greater sweep of material to be relevant and inform that decision than the majority did. The majority looked only to the contractual rights and obligations created.*

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## I INTRODUCTION

It is a pleasure to contribute to this special issue celebrating Professor John Prebble's extensive contributions to taxation research during his career. Professor Prebble has written extensively on the subject of tax avoidance. This article responds to and builds upon his 2006 book chapter "The *Peterson* Case and its Impact on the Rules in *BNZ Investments Ltd* and *Cecil Bros*".<sup>1</sup> That chapter analysed the Privy Council's 2005 *Peterson v Commissioner of Inland Revenue* decision,<sup>2</sup> arguing that while at first glance, the case may have looked like a "notable win" for the taxpayer, Mr Peterson, "in a broader context it was a major victory for the Commissioner of Inland Revenue ... and for taxpayers who do

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1 John Prebble "The *Peterson* Case and its Impact on the Rules in *BNZ Investments Ltd* and *Cecil Bros*" in Adrian Sawyer (ed) *Taxation Issues in the Twenty-First Century* (University of Canterbury Centre for Commercial and Corporate Law, Christchurch, 2006) 117 at 117.

2 *Peterson v Commissioner of Inland Revenue* [2005] UKPC 5, [2006] 3 NZLR 433.

not invest in shelters".<sup>3</sup> Indeed, Professor Prebble argued that the Commissioner "won every point of strategic significance".<sup>4</sup> The two most notable of these strategic wins were: first, that the Privy Council "put paid to several judicial heresies that threatened to enfeeble" the general anti-avoidance rule, or GAAR; and second, that:<sup>5</sup>

[p]erhaps even more importantly in the long run, their Lordships interpreted the legalistic deduction rule in [*Cecil Bros Pty Ltd v Federal Commissioner of Taxation*] almost into oblivion and recognised powers of apportionment in the Commissioner that no one [had] thought he possessed.

I have an interest in tax avoidance law, having written the textbook *Tax Avoidance Law in New Zealand*.<sup>6</sup> Beyond that, I have a particular interest in the *Peterson* case itself, having acted as junior counsel in the case. Written 15 years after Professor Prebble's chapter, this article concurs with Professor Prebble's analysis of the *Peterson* reasoning. In this article, I build on his 2006 chapter in several ways. First, in Part II, the article sets the scene by outlining the ratio of *Commissioner of Inland Revenue v BNZ Investments*.<sup>7</sup> As Professor Prebble's chapter astutely notes, overturning that ratio was a key goal for the Commissioner in *Peterson*. The next four Parts paint a detailed picture of the *Peterson* cases' procedural history, and the courts' reasoning and analysis, from the initial Taxation Review Authority cases,<sup>8</sup> to the appeals before the High Court,<sup>9</sup> then Court of Appeal,<sup>10</sup> and finally to the Privy Council.<sup>11</sup> This detailed analysis allows the reader to see what happened in the various stages of the *Peterson* litigation as the Commissioner tried to grapple with the effects of the Court of Appeal's judgment in *BNZ Investments*.

In this article, I also build upon Professor Prebble's 2006 analysis by considering the relationship between the *Peterson* reasoning and the leading 2009 New Zealand tax avoidance case of *Ben Nevis Forestry Ventures Ltd v Commissioner of Inland Revenue*.<sup>12</sup> In Part VII, I argue that *Ben Nevis* actually follows *Peterson* in two ways. First, it adopts the analysis of both the majority and the

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3 Prebble "*The Peterson Case and its Impact on the Rules in BNZ Investments Ltd and Cecil Bros*", above n 1, at 117.

4 At 117.

5 At 117. See generally *Cecil Bros Pty Ltd v Federal Commissioner of Taxation* (1964) 111 CLR 430 (HCA).

6 James Coleman *Tax Avoidance Law in New Zealand* (2nd ed, CCH New Zealand, Auckland, 2013).

7 *Commissioner of Inland Revenue v BNZ Investments Ltd* [2002] 1 NZLR 450, [2009] NZCA 47.

8 Part III.

9 Part IV.

10 Part V.

11 Part VI.

12 *Ben Nevis Forestry Ventures Ltd v Commissioner of Inland Revenue* [2008] NZSC 115, [2009] 2 NZLR 289.

minority judgments in *Peterson* to the effect that the general anti-avoidance provision only applies when the purpose of the particular provision has been thwarted. Secondly, it uses the minority's less judicial approach in considering whether the purpose of the specific provision has been complied with or not. The minority allowed a greater sweep of material to be relevant and inform that decision than the majority did. The majority looked only to the contractual rights and obligations created.

## **II SETTING THE SCENE: THE BNZ INVESTMENTS DECISION**

Professor Prebble is correct in his article to note that, apart from the desire to win the *Peterson* case, the Commissioner's other great hope was to overturn the ratio of the *BNZ Investments* case.<sup>13</sup> The ratio of that case was that the word "arrangement", as it appears in the general anti-avoidance provision, requires a consensus, a meeting of minds between the parties involved as to what would happen.<sup>14</sup> For example, according to Richardson P:<sup>15</sup>

The definition of arrangement closely follows the meaning given to the composite expression "contract, agreement or arrangement" in *Newton*<sup>16</sup> and other decisions under the former s 108 and its Australian counterpart, s 260 of the Income Tax Assessment Act 1936. ... [A]n arrangement cannot exist in a vacuum. As did the former s 108, s 99 bites on an "arrangement made or entered into". It presupposes there are two or more participants who enter into a contract or agreement or plan or understanding. They arrive at an understanding. They reach a consensus.

And a few paragraphs later, Richardson J continued:<sup>17</sup>

In our view that reasoning is also applicable under s 99. In short, an arrangement involves a consensus, a meeting of minds between parties involving an expectation on the part of each that the other will act in a particular way. The descending order of the terms "contract, agreement, plan or understanding" suggests that there are descending degrees of enforceability, so that a contract is ordinarily but not necessarily legally enforceable, as is perhaps an agreement, while a plan or understanding may often not be legally enforceable. The essential thread is mutuality as to content. The meeting of minds embodies an expectation as to future conduct. There is consensus as to what is to be done.

At the time, I was acting for the Commissioner. My view was that the Court of Appeal's reasoning substantially reduced the efficacy of the general avoidance provision. It meant that arrangements could be structured so that the taxpayer gaining the tax advantage does not know all the steps in the

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13 Prebble "*The Peterson* Case and its Impact on the Rules in *BNZ Investments Ltd* and *Cecil Bros*", above n 1, at 128.

14 *Commissioner of Inland Revenue v BNZ Investments Ltd*, above n 7, at [43].

15 At [43].

16 *Newton v Federal Commissioner of Taxation of The Commonwealth of Australia* [1958] AC 450 (PC) (citation added).

17 *Commissioner of Inland Revenue v BNZ Investments Ltd*, above n 7, at [50].

arrangement and hence could be rendered immune from the effects of the general anti-avoidance provision. That was alarming and its application to the *Peterson* case was obvious.

### **III PETERSON CASES IN THE TAXATION REVIEW AUTHORITY (TRA)**

The procedural context was that there had already been two TRA decisions on the so-called "film cases".<sup>18</sup> The Commissioner had advanced three arguments:

- that some of the transactions within the arrangement were shams, such that there was a fraud on the investors;<sup>19</sup>
- that not all the film production costs could be depreciated because they were not genuinely incurred;<sup>20</sup> and
- that s 99, as it then was, applied.<sup>21</sup>

In the *Lie of the Land* case, all three arguments failed at the TRA level.<sup>22</sup> But in the *Utu* case, at the TRA level the arrangement was held to be a fraud on all the investors, and the Judge concluded that the partnership had not truly incurred the total production costs.<sup>23</sup> Because the sham argument succeeded in the *Utu* case, the Judge considered that s 99 was inapplicable.<sup>24</sup> In conceptual terms, the *Lie of the Land* and *Utu* cases were identical. But differing levels of evidential support in the two cases led to conflicting judgments.

In the *Utu* case, the TRA found in the Commissioner's favour but on the basis that the non-recourse loans were never made and hence constituted shams. The TRA said:<sup>25</sup>

... this was not a fixed price contract in the manner contended for by the objector. The documents make it clear that the investors owned the whole process (ironically for tax driven motives) and contracted with Utu Productions to make the film. The relationship was one of principal and agent. No doubt that the investors expected that the production and marketing costs would not exceed \$3,100,000 on the faith of

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18 Case U6 (1999) 19 NZTC 9,038 (TRA) [*Lie of the Land* (TRA)]; and Case U32 (2000) 19 NZTC 9,302 (TRA) [*Utu* (TRA)].

19 *Lie of the Land* (TRA), above n 18, at 9,053.

20 At 9,054.

21 At 9,057. See Income Tax Act 1976, s 99.

22 At 9,059.

23 *Utu* (TRA), above n 18, at 9,311.

24 At 9,312.

25 At 9,311 (emphasis added).

Blakeney's representations. In fact, the costs were substantially less, probably about \$1,948,000 (\$3,100,000 less the \$1,152,000 fraudulently claimed by Glitteron).

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The short answer under this head is that the film cost less to make by the amount submitted by the Commissioner and the objector *cannot deduct his share of losses which were never incurred*.

If the loans were never made and in fact were shams, then the depreciation deduction could not be taken for the sham portion. There was no need to invoke s 99 if the loan portions were shams. Although the TRA had found that the loans were a sham, there was a problem with that logic. The inherent conceptual difficulty with any sham argument is that the party alleging the sham has to show that both parties to the transaction knew that it was a sham.

Actual knowledge by both parties is very difficult for a third party like the Commissioner to demonstrate without a witness who can confirm mental state of each party. Here, no such witness could give direct evidence as to the parties' knowledge or lack thereof that the arrangement was a sham. Only indirect inferences could be drawn from documents.<sup>26</sup> Mr Peterson gave evidence that he had no knowledge of the dishonest component of the arrangement.<sup>27</sup> Hence there was a problem with the sham argument and the argument was not pursued in the High Court appeal in either case.

Both these TRA judgments were issued prior to the *BNZ Investments* High Court and Court of Appeal judgments, which were delivered on 10 July 2000 and 22 May 2001 respectively. The rationale of the *BNZ Investments* cases had a direct impact on the *Lie of the Land* and *Utu* film cases because in neither case did Mr Peterson know of all the machinations of the promoters to effect the tax result promised. The *BNZ Investments* case was not proceeding to the Privy Council so the *Peterson* cases provided a convenient fact pattern on which to attack the logic of the *BNZ Investments* decisions.

#### ***IV THE HIGH COURT APPEALS***

On appeal to the High Court, the Commissioner had to navigate the new tax landscape created by the *BNZ Investments* case. The first attempt at dealing with the logic of the *BNZ Investments* decision was tried in the *Lie of the Land* case. The High Court decisions in the *Peterson* cases were issued on 19 February 2002 in the case of *Lie of the Land* scheme,<sup>28</sup> and on 14 June 2002 in the case of *Utu* film scheme.<sup>29</sup> In the High Court appeals, the Commissioner lost the *Lie of the Land* case, but won

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26 *Utu* (TRA), above n 18, at 9,304–9,308. See also *Commissioner of Inland Revenue v Peterson* (2002) 20 NZTC 17,589 (HC) [*Lie of the Land* (HC)] at 17,600.

27 *Utu* (TRA), above n 18, at 9,308; and *Lie of the Land* (TRA), above n 18, at 9,045.

28 *Lie of the Land* (HC), above n 26.

29 *Peterson v Commissioner of Inland Revenue (No 2)* (2002) 20 NZTC 17,761 (HC) [*Utu* (HC)].

the *Utu* case. *BNZ Investments* required a consensus as to what happened,<sup>30</sup> and had talked about wilful blindness and tacit knowledge.<sup>31</sup> So, the Commissioner argued that Mr Peterson had tacit knowledge of, and was wilfully blind as to, the steps put in place by Mr McLean.<sup>32</sup>

That was the fatal flaw in the argument advanced in the *Lie of the Land* High Court appeal. The argument should have simply been put on the basis that there was an arrangement that met the *BNZ Investments* test and that Mr Peterson was simply a person affected by the arrangement such that s 99(3) was engaged, even though he was not a party to the arrangement. There was plainly an arrangement because Mr McLean conceived of the plan and put it into effect and controlled the companies and all the steps that were taken.<sup>33</sup> The mistake was in arguing that Mr Peterson was a *party* to that arrangement rather than merely a *person affected* by an arrangement to which s 99(3) applied.

In the *Lie of the Land* High Court appeal, the deduction argument was dismissed as well. It was held that both the amounts which the investors invested and the amounts that they borrowed comprised the cost of the film and the depreciation base.<sup>34</sup>

The Commissioner learned from her mistake in the *Lie of the Land* High Court appeal and made the "person affected" argument in the second High Court appeal involving *Utu*. The Commissioner said that Mr Peterson was a person affected by a tax avoidance arrangement.<sup>35</sup> Therefore the Commissioner could make an adjustment against Mr Peterson's income under s 99(3) of the Income Tax Act 1976.<sup>36</sup>

It was still necessary that the Commissioner demonstrate an arrangement that would be caught by s 99. In this respect, it was argued for the Commissioner that there was an arrangement that met the test of *BNZ Investments*.<sup>37</sup> Mr Blakeney was at the centre of the *Utu* arrangement, and his plan was to inflate the price of the film. In addition to Mr Blakeney, the other parties to the arrangement were Glitteron Films Limited, Utu Funding Limited and Utu Productions Limited. In one way or another, Mr Blakeney controlled all of the companies that were parties to the arrangement.<sup>38</sup>

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30 *Commissioner of Inland Revenue v BNZ Investments Ltd*, above n 7, at [50].

31 At [26].

32 *Lie of the Land* (HC), above n 26, at 17,599.

33 At 17,598 and 17,599.

34 At 17,598 and 17,601–17,602.

35 *Utu* (HC), above n 29, at 17,764.

36 At 17,764.

37 At 17,772.

38 At 17,772.

One could visually sketch the arrangement as looking like a lollipop, the circular top consisting of the companies around which the money flowed, and with Mr Blakeney being at the centre. Mr Peterson and the other investors were like the stick at the bottom of the lollipop: they did not know the full extent of Mr Blakeney's skulduggery in the circular lollipop part of the arrangement's structure.

The Commissioner argued that this was a standard inflated deduction arrangement of the sort already proscribed by the Court of Appeal in *Wisheart, Macnab and Kidd v Commissioner of Inland Revenue* and hence amounted to a tax avoidance arrangement.<sup>39</sup>

The Commissioner's strategy worked. Despite the earlier judgment in the *Lie of the Land* case, Hammond J had no problem holding that the arrangement involved the necessary mutuality.<sup>40</sup> The only issue was whether s 99(3) applied to enable an adjustment to be made against Mr Peterson. That section applies whether or not the person was a party to the arrangement. It was not being alleged that Mr Peterson was a party; hence the issue of knowledge was irrelevant. The Judge held that subs (3) applied and the assessment was correct.<sup>41</sup>

## V THE APPEALS TO THE COURT OF APPEAL

At the end of the High Court litigation, both parties had won a case and lost a case. Both cases were appealed to the Court of Appeal.<sup>42</sup> Both *Peterson* Court of Appeal judgments were delivered on 19 February 2003. In both cases, the Commissioner advanced the same s 99 argument that had prevailed for the Commissioner in the *Utu* High Court case. The Commissioner did not rely on a sham argument, nor on any deduction arguments.

In the *Lie of the Land* case, the Court of Appeal began by describing the facts in considerable detail.<sup>43</sup> Having done so the Court said that it was not surprising that the Commissioner formed the view that this was an arrangement.<sup>44</sup> The Court then had to consider whether Mr Peterson is a person affected under s 99(3).<sup>45</sup>

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39 At 17,773. See generally *Wisheart, Macnab and Kidd v Commissioner of Inland Revenue* [1972] NZLR 319 (CA).

40 *Utu* (HC), above n 29, at 17,773.

41 At 17,773–17,774.

42 *Commissioner of Inland Revenue v Peterson* [2003] 2 NZLR 77 (CA) [*Lie of the Land* (CA)]; and *Peterson v Commissioner of Inland Revenue* (2003) 21 NZTC 18,069 (CA) [*Utu* (CA)].

43 *Lie of the Land* (CA), above n 42, at [6]–[19].

44 At [20].

45 At [27]–[28].

In the High Court *Utu* case, once it had been established that Mr Peterson was a person affected under s 99(3), the Court simply found for the Commissioner. Contrastingly, after hearing the s 99(3) argument, the Court of Appeal re-introduced the deduction aspect.<sup>46</sup>

We consider that the concentration by the TRA and the High Court on the lack of knowledge of the taxpayer and the accountant for the partnership meant that the crucial issue in the case was obscured. In our view that crucial issue is whether or not the loan from Steadfold to the partnership was repaid as the Commissioner decided. We think the evidence overwhelmingly indicates that the loan was advanced on the basis that the funds would be returned the same day and that occurred. Certainly the taxpayer has not shown that the evidence on which the Commissioner has quite reasonably relied is wrong and that the loan remains owing.

The decision of the TRA seems to rest on reasoning that because the loan was advanced it remains owing. The judgment of the High Court reasons that because the knowledge of the general partner could not be attributed to the taxpayer, the belief by the taxpayer that the loan still was repayable (in the event that the film generated returns) was sufficient.

Suddenly, the Australian case *Cecil Bros* was back in play.<sup>47</sup> The straight deductibility argument was back in focus. The Court of Appeal considered that the evidence left open the conclusion that the amount of the non-recourse loan had been returned to Steadfold in repayment of it and therefore the partnership's loan obligation did not form part of the cost of the film.<sup>48</sup> The Court said that by the time the case arrived in the Court of Appeal it was "enmeshed" in the complexities of s 99.<sup>49</sup>

Having raised this point, the Court then returned to the s 99 analysis and agreed that Mr Peterson was a person affected for the purpose of s 99(3).<sup>50</sup> Consequently, the Commissioner won using the same logic that had succeeded in the High Court in the *Utu* case. The trouble was that the *Cecil Bros* issue had been raised and it was destined to become the major issue in the appeal to the Privy Council.

In the *Utu* judgment, the s 99(3) logic was applied and Mr Peterson's appeal dismissed. That was the only argument raised by the Commissioner and she was content to go with that alone. However, the Court of Appeal also raised the issue of whether a simpler logic based on a deduction argument might have also been available. To the extent that the \$3.1 million costs to the partnership comprised the partnership taking on liability for loans that were not incurred or incurred only briefly and then

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46 At [31]–[32].

47 *Cecil Bros Pty Ltd v Federal Commissioner of Taxation*, above n 5.

48 *Lie of the Land* (CA), above n 42, at [34].

49 At [35].

50 At [47].

extinguished, the arrangement could be disregarded.<sup>51</sup> In other words, there was obiter comment to the effect that the deduction argument would have succeeded.

## VI THE PRIVY COUNCIL

Mr Peterson appealed both cases to the Privy Council. David Milne QC was instructed as lead counsel for the Crown. The Commissioner's argument was that there was no need for there to be a consensus or a meeting of minds for there to be an arrangement, and nor did the taxpayer have to be a party. The only arguments advanced were under s 99. Neither the sham nor the deduction arguments were resurrected. However, that did not stop the majority deciding the case using a logic that fitted the deduction basis more than the s 99 analysis.

Once Mr Milne QC was made aware of the composition of the Court, he was concerned. That was because England had had its own film cases litigation in *Ensign Tankers (Leasing) Ltd v Stokes (Inspector of Taxes)*.<sup>52</sup> That case involved quite similar facts to the *Peterson* cases. A partnership had invested 25 per cent of the cost of making a film with the remaining 75 per cent being borrowed by the partnership from a production company. The amounts lent to the partnership by the production company were paid into a bank account, but on the same day a payment of the same amount was made to the production company. The partnership claimed to deduct the entire production costs as its share of the "first-year allowances".

In that case, the House of Lords considered that the self-cancelling nature of the "purported" loans from the production company could not be said to be part of the cost of producing the film. The reason for Mr Milne QC's concern was that at first instance in *Ensign Tankers*, the presiding Judge was Lord Millet.<sup>53</sup> He had decided in favour of the taxpayer in that case. The Crown had appealed to the English Court of Appeal and won.<sup>54</sup> The taxpayer, having lost, then appealed that decision to the House of Lords.<sup>55</sup>

Lord Millet wrote the majority Privy Council judgment in *Peterson*.<sup>56</sup> The majority judgment explicitly accepted the proposition that s 99 applies when, but for its provisions, the impugned arrangement would meet all the specific requirements of the tax legislation.<sup>57</sup> The majority then

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51 *Utu* (CA), above n 42, at [13].

52 *Ensign Tankers (Leasing) Ltd v Stokes (Inspector of Taxes)* [1992] 1 AC 655 (HL).

53 *Ensign Tankers (Leasing) Ltd v Stokes (Inspector of Taxes)* [1989] 1 WLR 1222 (Ch).

54 *Ensign Tankers (Leasing) Ltd v Stokes (Inspector of Taxes)* [1991] 1 WLR 341 (CA).

55 *Ensign Tankers (Leasing) Ltd v Stokes (Inspector of Taxes)* (HL), above n 52.

56 *Peterson v Commissioner of Inland Revenue*, above n 2. See also Blair Keown "What's a Supreme Court to do? *CIR v Peterson* (2005) 22 NZTC 19,098 (PC)" (2006) 12 Auckland UL Rev 194.

57 *Peterson v Commissioner of Inland Revenue*, above n 2, at [4] per Lord Millet. See discussion in Prebble "*The Peterson Case and its Impact on the Rules in BNZ Investments Ltd and Cecil Bros*", above n 1, at 125.

brought the case back to the deduction arena. They introduced the shorthand \$x for the money that the investors put in and \$y for the amount of the non-recourse loan.<sup>58</sup> Millet LJ said that the Commissioner never gave a satisfactory answer to the appellant's argument that they paid \$x + \$y to acquire a film.<sup>59</sup> He further stated that:<sup>60</sup>

At no stage did the commissioner contend that, if they did pay the whole of that sum, they did not pay \$y as consideration for the acquisition of the film but paid it for some other purpose.

None of that is relevant to a tax avoidance analysis. It is relevant to the deduction argument that was not being run by the Commissioner.

The majority then turned to the Commissioner's tax avoidance analysis. Their Lordships took it for granted that the word "arrangement" does not require a consensus or meeting of the mind and nor does the taxpayer need to be a party to it.<sup>61</sup> So the objective of overturning the ratio from *BNZ Investments* was achieved.

The majority was satisfied that the "arrangement" which the Commissioner identified had the purpose or effect of reducing the investor's liability to tax; whether or not the investors were parties to the arrangement, they were affected by it.<sup>62</sup> One might be forgiven for thinking that, having made that finding, the application of s 99(3) was assured. However, that was not how things panned out.

The majority then added a qualification. They said that the crucial question is whether the tax advantage that the investors obtained amounted to "tax avoidance".<sup>63</sup> This, they said, was because not every tax advantage comes within tax avoidance as properly understood.<sup>64</sup> They then quoted from Lord Nolan in *Inland Revenue Commissioners v Willoughby*:<sup>65</sup>

The hallmark of tax avoidance is that the taxpayer reduces his liability to tax without incurring the economic consequences that Parliament intended to be suffered by any taxpayer qualifying for such reduction in his tax liability ... But it would be absurd in the context of [the provision there affording relief from tax] to describe as tax avoidance the acceptance of an offer of freedom from tax which Parliament has deliberately made.

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58 *Peterson v Commissioner of Inland Revenue*, above n 2, at [17] per Lord Millet.

59 At [20].

60 At [30].

61 At [34] per Lord Millet.

62 At [34].

63 At [35].

64 At [35].

65 At [38]. See *Inland Revenue Commissioners v Willoughby* [1997] 1 WLR 1071 (HL) at 1079.

The majority then reasoned that the scheme of the Act was that Parliament intended that film investors could depreciate the full acquisition cost of a film if they paid the \$x + \$y to acquire the film. The considered that in that situation Parliament intended the deduction and s 99 could not interfere.<sup>66</sup> More analysis of the purpose of the Act ensued with the majority saying that, consistently with the statutory scheme, it is not only necessary but also sufficient that the taxpayer should have incurred the capital expenditure in acquiring the assets for the purposes of trade.<sup>67</sup>

It was said that the Commissioner's failing was that she never succeeded in showing that the investors had not suffered the economic burden of paying \$x + \$y in acquiring the film.<sup>68</sup> Hence s 99 could not operate to obviate the ability to depreciate.<sup>69</sup> In this respect, the majority drew direct parallels with *Europa Oil (NZ) Ltd v Commissioner of Inland Revenue*.<sup>70</sup>

Their Lordships' finding that the monies paid by the taxpayer company ... is deductible under section 111 as the actual price paid by the taxpayer company for its stock-in-trade under contracts for the sale of goods entered into with Europa Refining ... is incompatible with those contracts being liable to avoidance under [the predecessor of s 99]. In respect of these contracts the case is on all fours with [*Cecil Bros*] in which it was said by the High Court of Australia 'it is not for the Court or the commissioner to say how much a taxpayer ought to spend in obtaining his income.'<sup>71</sup>

The majority lay the blame for this outcome on how the Commissioner conducted her case. In the majority's view, the Commissioner should have ensured that the TRA was presented with sufficient evidence to allow certain factual findings to be made. Ironically, those factual conclusions could have been inferred in any event from the evidence before their Lordships.

The minority explicitly endorsed Thomas J's approach in *BNZ Investments*, rejecting the notion that there needs to be consensus in an arrangement.<sup>72</sup> The minority then analysed the key difficulty in applying a general anti-avoidance provision: the task of distinguishing between those tax advantages that are to be nullified and those that are permissible.<sup>73</sup>

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66 *Peterson v Commissioner of Inland Revenue*, above n 2, at [39].

67 At [42].

68 At [42]–[43].

69 At [42]–[43].

70 At [43]. See *Europa Oil (NZ) Ltd v Commissioner of Inland Revenue* [1976] 1 NZLR 546 (PC) at 556. See discussion in Prebble "The Peterson Case and its Impact on the Rules in *BNZ Investments Ltd* and *Cecil Bros*", above n 1, at 121–122.

71 *Cecil Bros Pty Ltd v Federal Commissioner of Taxation*, above n 5, at 434 (citation added).

72 *Peterson v Commissioner of Inland Revenue*, above n 2, at [58] and [59] per Lords Bingham and Scott.

73 At [60].

Where the minority differed from the majority was in articulating Parliament's purpose in the context of allowing depreciation relief. According to the minority, as a matter of principle, if the proceeds of the non-recourse loans have not been used to meet the costs of production, it cannot be said that the expense falls within the statutory purpose.<sup>74</sup> The IR 52.3 ruling operates here as a proxy for the statutory purpose.<sup>75</sup> If the money was not used to meet the production cost of the film, then the general anti-avoidance provision should apply.<sup>76</sup>

The minority then went through the facts and inferred that the investors had been duped.<sup>77</sup> The amount of the non-recourse loan had been returned to the lender. To conclude otherwise would be to shut one's eyes to the obvious.<sup>78</sup> The arrangement inflated the cost of the film. The minority considered that it was not within the scheme of the ruling for the cost of acquisition to be inflated for no commercial purpose other than to qualify for higher tax deductions. Hence there was a tax advantage of the sort that enabled the general anti-avoidance provision to apply.<sup>79</sup>

There is no disharmony in their Lordships' approach to how the general anti-avoidance provision is to apply. The disagreement regarded whether or not, on the facts, the Parliamentary purpose of the provision allowing the depreciation (in this case IR 52.3) had been met. The majority said it had and the minority said that it had not.

## VII THE INFLUENCE OF PETERSON ON BEN NEVIS

My contention is that the New Zealand Supreme Court effectively adopted the principal analysis of their Lordships in *Ben Nevis* but also adopted the broader approach to the evidence that the Privy Council minority used in *Peterson*.<sup>80</sup> In other words, the reasoning of both was amalgamated in *Ben Nevis*.

The general approach to tax avoidance adopted by both the majority and the minority of the Privy Council in *Peterson* was adopted in *Ben Nevis*. Writing for the majority, Tipping and McGrath JJ stated that:<sup>81</sup>

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74 At [65].

75 At [62].

76 At [65].

77 At [69].

78 At [78].

79 At [88].

80 *Ben Nevis Forestry Ventures Ltd v Commissioner of Inland Revenue*, above n 12.

81 At [106].

Put at the highest level of generality, a specific provision is designed to give the taxpayer a tax advantage if its use falls within its ordinary meaning. That will be a permissible tax advantage. The general provision is designed to avoid the fiscal effect of tax avoidance arrangements having a more than merely incidental purpose or effect of tax avoidance. Its function is to prevent uses of the specific provisions which fall outside their intended scope in the overall scheme of the Act. Such uses give rise to an impermissible tax advantage which the Commissioner may counteract. The general anti-avoidance provision and its associated reconstruction power provide explicit authority for the Commissioner and New Zealand courts to avoid what has been done and to reconstruct tax avoidance arrangements.

Tipping and McGrath JJ continued in this vein, stating that:<sup>82</sup>

The ultimate question is whether the impugned arrangement, viewed in a commercially and economically realistic way, makes use of the specific provision in a manner that is consistent with Parliament's purpose.

My contention that the broader, less legalistic approach to the facts as used by the minority in *Peterson* has been adopted in *Ben Nevis*, is borne out by the majority statement that:<sup>83</sup>

The general anti-avoidance provision does not confine the Court as to the matters which may be taken into account when considering whether a tax avoidance arrangement exists. Hence the Commissioner and the Courts may address a number of relevant factors, the significance of which will depend on the particular facts. The manner in which the arrangement is carried out will often be an important consideration. So will the role of all relevant parties and any relationship they may have with the taxpayer. The economic and commercial effect of documents and transactions may also be significant. Other features that may be relevant include the duration of the arrangement and the nature and extent of the financial consequences that it will have for the taxpayer. As indicated, it will often be the combination of various elements in the arrangement which is significant. A classic indicator of a use that is outside Parliamentary contemplation is the structuring of an arrangement so that the taxpayer gains the benefit of the specific provision in an artificial or contrived way. It is not within Parliament's purpose for specific provisions to be used in that manner.

That paragraph specifically sets out in a summary form the type of factors that the minority looked at in *Peterson* and avoids the overly judicial approach of the *Peterson* majority in determining whether the particular provision has been used in a manner consistent with Parliamentary contemplation. The majority had effectively confined the inquiry as to whether Parliament's purpose had been met to a legal analysis of the contractual arrangements. The minority looked more broadly at the economic and commercial substance of the arrangement.

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82 At [109] per Tipping and McGrath JJ.

83 At [108].

### ***VIII CONCLUSION***

In my opinion, the polarising analysis by their Lordships in *Peterson* had a direct effect on the Court in *Ben Nevis*. Without the absurdity of the majority result, the Supreme Court may not have been persuaded to adopt such an encompassing approach to the material that is relevant to the question of whether a particular provision has been used as contemplated by Parliament. That liberalising of the analytical framework from a tight judicial analysis of the rights and obligations in the contract, to the broader commercial and economic effects of the arrangement, was a huge milestone in tax avoidance law. As Professor Prebble foreshadowed in 2006, we have the disagreement in the *Peterson* case to thank for that.