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SMALL-SCALE PROPERTY DEVELOPMENT: GST IMPLICATIONS

Abstract

The purpose of this article is to explore the GST implications of small-scale property development in Australia and to provide guidance as to whether such activities give rise to a GST liability. The legislation governing the operation of the GST affecting these projects uses the familiar terminology of 'business', but it also uses terminology such as 'adventure or concern in the nature of trade', which has not received extensive consideration by the Australian courts. The authors review relevant case law to identify key principles, which will guide the courts in applying this terminology to small-scale property development, and provide guidance as to when a taxpayer undertaking such projects will be required to register for GST. The authors also discuss the factors relevant to determining the impact of the timing of registration. The article concludes that small-scale property developers need to be aware of the complexities and uncertainty in relation to the application of the GST to such projects.

I Introduction

The GST has now been with us for over a decade. Although its day-to-day applicability is mostly well-known, its application is less clear in the case of small-scale property developments, which are not uncommon amongst taxpayers whose primary income is from salary and wages. There are many variants of what encompasses a small-scale development but a typical scenario involves buying a run-down house, demolishing it, subdividing and building multiple dwellings on the site. The case law concerning this issue is not clearly resolved which means that neither the advisors nor the taxpayer can be certain as to whether or not the sale of the developed property will give rise to a GST liability. Given that the sale price of the property is determined by market forces and that the GST cannot be arbitrarily added to the sale price, it is important that the taxpayer has a greater degree of certainty regarding the liability to GST for compliance purposes and for assessing the viability of the project.

This article reviews the relevant legislation and case law applicable to the potential GST liability of small-scale property development. Part II examines the meaning

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of ‘carrying on an enterprise’ and the requirements to register for the GST. Registration for the GST is a necessary though not sufficient condition for there to be a GST liability on the sale proceeds from the development. If registration is not required and not voluntarily undertaken, there will be no GST liability on such sales. Part III of this article considers the consequences of registration and what effect the timing of registration has on the liability to pay GST.

II When Will There Be a Potential Liability to Pay GST?

A *Legislative Background*

Under s 7-1 of *A New Tax System (Goods and Services Tax) Act 1999* (Cth) (‘*GSTA*’) there will be a GST liability where a taxpayer makes a ‘taxable supply’. Section 9-5 of the *GSTA* states:

> You make a ***taxable supply*** if:
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> (a) you make the supply for *consideration; and
>
> (b) the supply is made in the course or furtherance of an *enterprise that you *carry on; and
>
> (c) the supply is *connected with the indirect tax zone; and
>
> (d) you are *registered, or *required to be registered.
>
> However, the supply is not a *taxable supply to the extent that it is *GST-free or *input taxed.

The requirements in sub-ss (a), (c) will generally be fulfilled for small-scale developers,[1] which leaves the more contentious issue of whether GST registration is required. If GST registration is required, sub-s (d) will be fulfilled as will sub-s (b) because carrying on an enterprise is a prerequisite for GST registration.[2]

In general, GST registration is required when a taxpayer carries on an enterprise and has a GST turnover which exceeds the turnover threshold.[3] Consequently, the two main issues relevant in deciding whether small-scale property developers need to be registered for GST are whether they are carrying on an enterprise and the amount of their GST turnover.

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1 The requirements in *GSTA* s 9-5(a) will be fulfilled because supplying real estate constitutes a supply under *GSTA* s 9-10. Furthermore, the receipt of money will constitute consideration under *GSTA* s 9-15. The requirement of s 9-5(c) will also be fulfilled as real estate located in Australia will be regarded as being connected with the indirect tax zone under *GSTA* s 9-25(4).

2 Ibid s 23-5.

3 Ibid ss 23-5, 23-15.

B *Carrying on an Enterprise*

Section 9-20(1) of the *GSTA* defines an 'enterprise' as follows:

> (1) An ***enterprise*** is an activity, or series of activities, done:
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> (a) in the form of a *business; or
>
> (b) in the form of an adventure or concern in the nature of trade; or
>
> (c) on a regular or continuous basis, in the form of a lease, licence or other grant of an interest in property; or
>
> (d) by the trustee of a fund that is covered by, or by an authority or institution that is covered by, Subdivision 30-B of the **ITAA 1997* and to which deductible gifts can be made; or
>
> (da) by a trustee of a *complying superannuation fund or, if there is no trustee of the fund, by a person who manages the fund; or
>
> (e) by a charity; or
>
> (g) by the Commonwealth, a State or a Territory, or by a body corporate, or corporation sole, established for a public purpose by or under a law of the Commonwealth, a State or a Territory; or
>
> (h) by a trustee of a fund covered by item 2 of the table in section 30-15 of the *ITAA 1997* or of a fund that would be covered by that item if it had an ABN.

Of relevance to this article is the inclusion of activities 'in the form of a business' or 'in the form of an adventure or concern in the nature of trade'.[4] As the definition of enterprise is an exhaustive definition it does not require the courts to consider the ordinary meaning of the term 'enterprise', but it does leave to interpretation the meanings of the phrases 'in the form of a business' and 'in the form of an adventure or concern in the nature of trade'. In addition, s 9-20(2)(a) excludes from the meaning of enterprise a person as an employee, s 9-20(2)(b) excludes any private recreational pursuit or hobby and s 9-20(2)(c) makes it clear that individuals and partnerships of individuals will only meet the definition of enterprise if there is a reasonable expectation of profit or gain. Given the unfamiliarity of some of these terms in Australian tax law it is necessary to examine other jurisdictions to consider their meaning in relation to the *GSTA*. This needs to be done with some caution, however, given that there are significant differences in the equivalent legislation in other jurisdictions.[5]

Application of s 9-20 to small-scale developments raises a number of important issues including: the extent to which this section could apply to one-off undertakings; whether the phrase 'in the form of' adds to the scope of the terms 'business' and 'an adventure or concern in the nature of trade'; and whether 'an adventure or

4 Ibid ss 9-20(1)(a)–(b).

5 Richard Krever, *GST Legislation Plus 2014* (Thomson Reuters, 2014) 75–6.

concern in the nature of trade' is significantly different from the notion of 'business' as used in the *Income Tax Assessment Act 1997* (Cth) ('*ITAA97*'). Although the Australian Taxation Office has a number of private rulings concerning whether land developers are carrying on an enterprise, these rulings are often inconsistent, further adding to the confusion faced by taxpayers.[6] Furthermore, it has been argued that some case law suggests that a court's decision as to whether the taxpayer is 'carrying on an enterprise' is primarily based on the court's overall impression of the taxpayer's activities.[7]

1 *Whether Single Transactions are Potentially Covered by the GSTA*

Both the *GSTA* and *A New Tax System (Australian Business Number) Act 1999* (Cth) ('*ABNA*') use the phrase 'activity, or series of activities' in relation to the definition of an enterprise but neither Act defines this phrase. This raises the question of whether the scope of this phrase includes a single transaction. The New Zealand GST legislation also uses the term 'activity' and defines a 'taxable activity' as 'any activity which is carried on continuously or regularly'.[8] This definition arguably removes the application of GST in New Zealand from a one-off purchase and sale of property.

The meaning of 'activity' under s 6(1) of the *Goods and Services Tax Act 1985* (NZ) was considered in the New Zealand decision in *Newman v Commissioner of Inland Revenue.*[9] In *Newman v CIR* the taxpayer, who was registered for GST as a builder, purchased a 2.7 hectare block of land and commenced building a house to be used as the family home. The house was only partly completed when the family moved in. At that time the taxpayer was experiencing financial difficulty and, as a result, he subdivided and sold part of the 2.7 hectare block. The Commissioner argued that the sequence of steps required for planning, seeking approval, carrying out works and selling the land constituted an activity which was carried on continuously and regularly.[10] The New Zealand Court of Appeal unanimously disagreed with the Commissioner's argument and thereby found that the subdivision was not an activity that was carried on continuously or regularly and therefore was not a taxable activity. Justice Richardson concluded:

> The activity engaged in by the appellant in relation to this land to provide the front lot for sale was, on the evidence, a straightforward subdivision. There was no development work on the property. The activity was not repeated over time

6 Chris Sievers, *GST and 'Enterprise' in the Context of the Sub-division and Sale of Real Property* (30 March 2012) All About GST in Australia <http://chrissievers.com/gst-and-enterprise-in-the-context-of-the-sub-division-and-sale-of-real-property/>.

7 Melanie Baker, 'Tutors, Motor Vehicle Enthusiasts and Litigation Funders: A Case Update on What it Means to "Carry on an Enterprise"' (2014) 14(2) *Australian GST Journal* 30, 38.

8 *Goods and Services Tax Act 1985* (NZ) s 6(1)(a).

9 (1995) 17 NZTC 12 097 ('*Newman v CIR*').

10 *Goods and Services Tax Act 1985* (NZ) s 6(1)(a) defines 'taxable activity' as meaning 'any activity which is carried on continuously or regularly'.

> either continuously or regularly. It did not involve repeated acts. Dissection of what was done into a series of sequential steps does not answer the statutory test of whether the activity was carried on continuously.[11]

Importantly, the Court of Appeal considered the project as one activity and rejected the Commissioner's argument that the subdivision consisted of a series of activities.

However, it appears unlikely that the Australian courts would follow the New Zealand approach, given the differences that exist between the legislation. First, the use of the phrase 'activity, or series of activities' in s 9-20 suggests that a singular activity is distinct from an ongoing series of activities and that both can constitute an enterprise. Furthermore, in contrast to the New Zealand legislation, the Australian legislation does not limit the general definition of enterprise with the phrase 'continuously or regularly', although the Australian legislation uses this phrase in relation to the specific activities involving 'a lease, licence or other grant of an interest in property'.[12] As this phrase is excluded from the other elements of the definition of enterprise, this could be taken as an indication that its omission was deliberate and that it was intended that all the other elements of s 9-20(1) apply to one-off transactions. This is supported by *Miscellaneous Taxation Ruling MT 2006/1* which sets out the Commissioner's view on the meaning of this phrase and states that 'the term "activity, or series of activities" for an entity can range from a single undertaking including a single act to groups of related activities or to the entire operations of the entity.'[13]

A related issue is raised where the legislation not only requires the presence of an enterprise, but also requires, in *GSTA* s 9-5(b), that 'the supply is made in the course or furtherance of an enterprise that you carry on'. When the GST was first introduced, it was argued that in the event that the present day courts adopt the notion that 'carrying on' requires an element of repetition, (and even if a one-off transaction constitutes an enterprise as defined by s 9-20) there is a case to argue that it may not meet the requirement of being carried on as it does not exhibit characteristics of repetition.[14] This view has support given that the definition of 'carrying on' was considered in *Smith v Anderson*[15] as 'a repetition of acts, and excludes the case of an association formed for doing one particular act which is never to be repeated'.[16]

11 *Newman v CIR* (1995) 17 NZTC 12 097, 12 101.

12 *GSTA* s 9-20(1)(c).

13 Australian Taxation Office, *The New Tax System: The Meaning of Entity Carrying on an Enterprise for the Purposes of Entitlement to an Australian Business Number*, MT 2006/1, 13 December 2006, [153] ('*Miscellaneous Taxation Ruling MT 2006/1*'). See for relevance to the GST: Australian Taxation Office, *Goods and Services Tax: Does MT 2006/1 Have Equal Application to the Meaning of 'Entity' and 'Enterprise' for the Purposes of the A New Tax System (Goods and Services Tax) Act 1999?*, GSTD 2006/6, 13 December 2006.

14 Justice D Graham Hill, 'Goods and Services Tax: Flagging for the Courts the Problems of the GST' (2000) 3(6) *Tax Specialist* 304.

15 (1880) 15 Ch D 247.

16 Ibid 277–8.

Subsequently, in the Australian Federal Court case of *Toyama Pty Ltd v Landmark Building Developments Pty Ltd*,[17] White J held that while the phrase 'in the form of a business' in *GSTA* s 9-20(1)(a) can include a one-off activity, the reference to 'an enterprise that you carry on' in *GSTA* s 9-5 does introduce a requirement of a series of acts.[18] However, his Honour gave a very lenient interpretation of the requirement of a series of acts and, on the facts, held that a trustee's actions concerning a single property, which included the use of consultants, marketing of the property, obtaining of advice and arranging the property's sale, were activities that fulfilled this requirement.[19]

In summary, it appears that a one-off development potentially falls into the GST net. However, the following discussion does indicate that in some circumstances a one-off transaction (all things equal) is less likely to fulfil the requirement of an 'enterprise' under *GSTA* s 9-20(1)(a).

2 *In the Form of a Business*

An activity or a series of activities constitutes an enterprise if they are in the form of a business.[20] The term 'business' is further defined in the *GSTA* as including 'any profession, trade, employment, vocation or calling, but does not include occupation as an employee.'[21] This definition is identical to that used in s 995-1 of the *ITAA97* and therefore it is reasonable to presume that the extensive body of income tax case law relating to this definition will be applied in relation to GST.[22] Unlike the *ITAA97*, however, the definition of an 'enterprise' used in *GSTA* s 9-20(1) prefaces the term 'business' with the words 'in the form of'. This raises the issue of whether the inclusion of this phrase extends the meaning of 'business' beyond the case law established from income tax decisions. This issue is discussed later in this part of the article. First, however, it is necessary to examine how the current income tax decisions may influence the courts in relation to defining 'business' for GST purposes and how they impact the GST liability of small-scale property development.

As an inclusive definition, the courts are open to consider the ordinary meaning of the term 'business' as well as its statutory meaning. As a result, the case law has given rise to a range of indicia that are commonly considered when distinguishing between a business activity and a recreational pursuit. According to case law arising from income tax decisions, an operation will constitute a business when it has certain indicia, including: being organised in a business-like manner, the taxpayer has a

17 (2006) 197 FLR 74.

18 Ibid 87–8.

19 Ibid.

20 *GSTA* s 9-20(a).

21 Ibid s 195-1 (definition of 'business').

22 *Rendyl Properties Pty Ltd v Federal Commissioner of Taxation* (2009) ATC 2870, 2873–4.

profit intention, the activity involves repetition and the size of the activity is beyond that needed for personal needs.[23] It is not necessary for an operation to have all these indicia to constitute a business as the courts have still held that a business is being conducted even though some indicia are not present.[24]

In the case of a taxpayer repeatedly developing and selling property, there is a strong case that the taxpayer is carrying on a business. This is because, in such circumstances, there is both an intention to resell the property at the time of purchase and a repetition of similar transactions, both of which are important though non-determinative indicators that the taxpayer is carrying on a business.[25] In the case of *Crow v Federal Commissioner of Taxation*[26] a taxpayer who had repeatedly purchased and subdivided land was held by Lockhart J to be carrying on a business of property development. Although the Court in *Crow* found that the taxpayer had an intention to resell at the time of purchasing the property, the Court also placed importance on the fact that the taxpayer had undertaken many developments, as well as the systematic nature of the developments undertaken.[27] Whilst this case involved developments that were typically several hundred acres each, there is reason to believe that its findings could be applicable to small-scale developers where the land developed would be substantially smaller in size. Importantly, courts have made it clear that the volume of operations and capital alone are generally far from decisive in determining whether an operation is a business.[28] Consequently, a taxpayer who has a history of small-scale property development through buying, developing and selling a property carries most of the salient features that were present in *Crow* and would likely be seen as carrying on a business.

In contrast, there is much less certainty about whether a business is carried on where a developer who bought property without an intention to resell it subsequently undertakes an isolated development which they then sell. This uncertainty is due

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23 *Ferguson v Federal Commissioner of Taxation* (1979) 37 FLR 310.

24 For instance, in the case of *Federal Commissioner of Taxation v Walker* (1985) 79 FLR 161, a relatively small operation that originally involved one Angora goat was held to be a business. In the case of *Federal Commissioner of Taxation v Stone* (2005) 222 CLR 289, the High Court held that a sportsperson was carrying on a business despite the lack of a profit intention.

25 See *Federal Commissioner of Taxation v Swansea Services Pty Ltd* (2009) 72 ATR 120 ('*Swansea*') regarding how an intention to profit upon purchasing an asset can weigh in the finding that the taxpayer is carrying on a business. See also *Federal Commissioner of Taxation v St Hubert's Island Pty Ltd* (1978) 138 CLR 210, 246 [21] regarding the importance of repetition in finding that the taxpayer was carrying on a business.

26 (1988) 19 ATR 1565 ('*Crow*').

27 Ibid 1573.

28 See, eg, the following cases which found the presence of a business despite relatively small amounts of money involved: *Federal Commissioner of Taxation v Walker* (1985) 79 FLR 161; *Ferguson v Federal Commissioner of Taxation* (1979) 37 FLR 310; *Thomas v Federal Commissioner of Taxation* (1972) 46 ALJR 397.

to limited relevant case law, and although *Taxation Ruling TR 92/3* attempts to give some guidance on this issue, it is of limited assistance and has been subject to some criticism.[29]

One of the earlier Australian cases that held that an isolated transaction can be regarded as a business is *Federal Commissioner of Taxation v Whitfords Beach Pty Ltd*.[30] Although this case involved a large-scale professional development, its findings are relevant in deciding whether a small-scale developer is conducting a business. The taxpayer in this case was a company initially incorporated to purchase 1584 acres of beachfront land for recreational purposes. Thirteen years later the shares in Whitfords Beach Pty Ltd were purchased by three companies which had a history of property development and clearly intended to subdivide and develop the land. The new owners amended the Articles of Association of the taxpayer and proceeded to develop the property. This development involved rezoning and subdividing the land, as well as an extensive physical development, including building roads and the installation of drainage, electricity, water and sewerage. The High Court, by majority, held that the gain was ordinary income due to the taxpayer now being in the business of developing the land. This was despite the taxpayer having undertaken one development rather than a continuing series of developments. The conclusion of two of the three majority judges appeared to be highly influenced by the extensiveness of the development.[31] Their Honours indicated that a previous High Court case that had found on similar facts that there was no business might not be considered good law.[32] Although the judges did not state how extensive a development would have to be to constitute a business, they did state that merely subdividing the land would of itself be insufficient.[33]

Unfortunately, since the decision in *Whitfords Beach*, only a small number of cases have considered whether an isolated property development venture would constitute a business or a mere realisation of a capital asset. In the Full Federal Court decision of *Statham v Federal Commissioner of Taxation*,[34] the taxpayer was the trustee of a deceased estate. The deceased in question had originally operated a farming business on a property of approximately 270 acres. As the farming activities had not been financially viable, the deceased had subdivided the land, carried out earthworks, constructed roads and connected the lots to the electricity grid. The trustee did

[29] Australian Taxation Office, *Income Tax: Whether Profits on Isolated Transactions are Income*, TR 92/3, 30 July 1992 (‘*Taxation Ruling TR 92/3*’). For criticism of *Taxation Ruling TR 92/3*, see R C Allerdice, ‘*Ruling TR 92/3*: The Voice of the Profit’ (1993) 27 *Taxation in Australia* 408; Julie Cassidy, ‘The Taxation of Isolated Sales under Section 25(1) *ITAA*: *TR 92/3* v Joint Submission’ (1994) 4 *Revenue Law Journal* 1, 17–18; Rami Hanegbi, ‘Isolated Transactions: Current Income Tax Implications’ (2006) 35 *Australian Tax Review* 248, 256–7.

[30] (1982) 150 CLR 355 (‘*Whitfords Beach*’).

[31] Ibid 384–5 (Mason J), 399–400 (Wilson J).

[32] Ibid 385 (Mason J), 398 (Wilson J).

[33] Ibid 385 (Mason J), 400 (Wilson J).

[34] (1988) 20 ATR 228 (‘*Statham*’).

not directly contract with any party that developed the land and was not directly involved in selling the land, but rather assigned this task to a real estate agent. Over a number of years, 105 lots were sold for a total of over $1.1 million. The Full Federal Court held that the taxpayer was not running a business of land development but merely realised a capital asset, albeit at its best value. In its decision, the Court was particularly influenced by the 'hands-off' approach of the taxpayer; the process of development and sale was left to other parties.[35] The Court was also influenced by the limited nature of the physical development.[36] As a consequence, it has been suggested that *Statham* supports the view that a one-off project can avoid being labelled a business for tax purposes if the taxpayer does not actively participate in the process of developing and selling the property.[37]

The decision in *Statham* has more recently been supported by the decision of a single judge of the Federal Court in *Casimaty v Federal Commissioner of Taxation*.[38] In this case, the taxpayer had farmed land of approximately 1000 acres. The land had originally been gifted to him by his father, but the taxpayer was unable to make sufficient money from farming to support his debts, so over a number of years the taxpayer developed and sold approximately two-thirds of the land. The taxpayer not only subdivided the land but also constructed roads, provided water and sewerage facilities to the blocks, and built external fencing. While the development was extensive, the taxpayer only developed the land to the extent that the taxpayer needed to obtain council approval for subdivision. Justice Ryan held that the development activities did not constitute a business. His Honour, however, did indicate that had the development process been more extensive it would have been easier to find that the taxpayer was running a business.[39] His Honour specifically indicated that this might have been the case had the taxpayer built fences or units on the blocks and been more directly involved in the sales process.[40]

Conversely, in *Stevenson v Federal Commissioner of Taxation*[41] a single judge of the Federal Court found that an isolated development did constitute a business. This case also involved a taxpayer who had farmed land for many years but subsequently ceased farming, subdivided the area into smaller lots and sold them over several years. The project was undertaken in stages, and involved a total of 360 acres and receipts of over $3 million. As well as subdividing the land, the taxpayer arranged works for the supply of water, sewerage reticulation and power to each of the blocks. One stage included developing a park with a public toilet, as well as construction of a seawall where the blocks fronted a lake. Two of the stages also involved road

35 Ibid 235–6.

36 Ibid 235.

37 Geoffrey Hart, 'The Limited Impact of *Whitfords Beach* in Urban Land Development' (2007) 17 *Revenue Law Journal* 85, 94–8.

38 (1997) 151 ALR 242 ('*Casimaty*').

39 Ibid 261–2.

40 Ibid.

41 (1991) 29 FCR 282.

works and one also involved earth works. Unlike the cases of *Statham* and *Casimaty*, the taxpayer was directly involved in the development and sales process. He was also the sole decision-maker, controlled the marketing of the blocks and, on many occasions, dealt directly with purchasers. The taxpayer also dealt directly with the council and other authorities, and, occasionally, even did some work on the land himself to avoid paying for labour. In finding that the taxpayer was conducting a business, Jenkinson J placed particular importance on the fact that the taxpayer personally undertook much of the planning and management of the development.[42] His Honour also approved the principle stated by Mason J in *Whitfords Beach*: the extent of the development activities is an important consideration in determining whether the taxpayer is in business or not.[43]

An isolated development project was also held to be a business by the single judge Federal Court case of *Abeles v Federal Commissioner of Taxation*.[44] In this case, two brothers purchased 10 acres of land. Upon the land being rezoned, they entered into a development that involved not only their land but also the neighbouring land. In total, the development involved six different pieces of land and four groups of land owners. The costs of the development were shared on a pro-rata basis, and the development involved not only subdividing the land, but also road, sewerage and other works. The brothers eventually sold 38 blocks of land, most of them in one year. Justice O'Loughlin held that the taxpayers were carrying on a business of development. His Honour's decision was based on the extensiveness of the development and that the brothers had participated in the development together with the owners of the neighbouring properties, which gave it a business-like character.[45] Although his Honour's decision was also influenced by his determination that the property was not initially purchased for domestic purposes, this decision was ultimately made without being able to identify the dominant purpose of the purchase.[46]

These abovementioned cases are of importance in relation to whether a taxpayer, who has purchased property without an intention to develop it but then subsequently undertakes an isolated development on that property, will be found to meet the definition of 'enterprise' and potentially require registration for GST. In particular, the key factors that will be considered are the taxpayer's level of involvement in the development and sale process, and the extent of the work done to carry out the development.[47] Nevertheless, under the current case law, it remains uncertain in many specific situations whether an isolated development project will constitute a business.

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42 Ibid 290.

43 Ibid 291–2.

44 (1991) 22 ATR 504.

45 Ibid 512.

46 Ibid. Although the taxpayers claimed that they had purchased the property for domestic purposes (as a residence for themselves) this claim was met by the judge with scepticism.

47 For a contrary view that argues that isolated transactions are highly unlikely to constitute a business, see Hart, above n 37.

Another important 'intermediate' scenario to consider is that of a one-off small-scale developer who acquires a property with an intention to develop and sell, and then subsequently acts out their intention. While there is very little case law that considers whether such a taxpayer's activities constitute a business, to a large degree this issue is redundant because, as discussed in this paper, such activities will typically fall into the GST net as constituting an 'adventure in the nature of trade'.[48] The limited case law suggests that the presence of a profit intention upon purchase will clearly strengthen the argument that such a taxpayer is also carrying on a business. The recent case of *Swansea*[49] illustrates how important the presence of a profit intention by resale upon purchase can be in determining whether a taxpayer is carrying on a business. *Swansea* concerned whether a long-term investment in paintings, artwork and antiques by a corporation was an enterprise for GST purposes. Justice McKerracher found that the investment activity was in the 'form of a business' even though long-term capital investments generally are not treated as a business for income tax purposes.[50] An important factor in this decision was that the facts supported the view that the painting, artwork and antiques were purchased with an intention to later sell at a profit.[51]

Much of the previous analysis (other than the discussion on *Swansea*) has relied on cases concerning income tax law to explore the meaning of the term 'business'. But, the income legislation does not use the phrase 'in the form of a business' as is the case with *GSTA* s 9-20(1)(a). It is, therefore, necessary to consider whether the addition of 'in the form of' has any significant impact on the way in which the term 'enterprise' is interpreted by the courts. In *Miscellaneous Taxation Ruling MT 2006/1*, the Commissioner suggests that the inclusion of this phrase gives a wider meaning to the word 'business' and, in particular, would include non-profit entities and smaller superannuation funds.[52] Justice McKerracher in *Swansea* also expressed the view that the phrase 'in the form of' extends the meaning of 'enterprise' beyond the ordinary meaning of 'business' and stated, in agreement with the comment in *Miscellaneous Taxation Ruling MT 2006/1*, that it includes activities that have the appearance or characteristics of business activities, but do not fall into the ordinary legal meaning of the term 'business'.[53] His Honour also noted that for an individual, the activity must still be intended to be profit-making and not a private recreational pursuit or hobby.[54]

In summary, in relation to a small-scale developer, it appears that those who repeatedly undertake developments would, in most instances, be carrying on a business and so

48 Although the legislation such as the *GSTA* s 9-20(1) uses the term 'adventure or concern in the nature of trade' case law uses this term interchangeably with 'adventure in the nature of trade'. See *Edwards (Inspector of Taxes) v Bairstow* [1956] AC 14, 25 ('*Edwards*').

49 (2009) 72 ATR 120.

50 Ibid 147.

51 Ibid.

52 *Miscellaneous Taxation Ruling MT 2006/1* [170B].

53 (2009) 72 ATR 120, 146–7.

54 Ibid.

would be regarded as carrying on an enterprise. Depending on the facts, however, taxpayers who undertake a development on a one-off or sporadic basis, who did not acquire their property with the intention of development, are in some situations either undertaking a business or at least undertaking activities that are 'in the form of a business'. In particular, the extent of the development and whether the taxpayer is directly involved in the project will be important in determining the outcome of a given case.[55] The Australian Taxation Office is of the view that the extensiveness of the development is very important in determining whether there is an enterprise being carried on. Specifically, the Australian Taxation Office believes that even where property has not been purchased with an intention to profit from resale, an extensive development to a large piece of land will constitute an enterprise, as will demolishing a house, subdividing the land and building two houses on the block.[56] On the other hand, where a property has not been purchased with an intention to resell it at a profit, the Australian Taxation Office is of the view that a subdivision that is accompanied with either minimal activity, or minimal work necessary to get the subdivision approved without building on the subdivided land will generally not constitute an enterprise.[57] The other possibility that needs to be considered is the 'intermediate' case of a one-off or sporadic development where the property was acquired with the intention of development. Although there is very limited case law that determines whether such taxpayers are carrying on a business or are undertaking activities 'in the form of a business', there will be a stronger case for this in comparison to when there is no such intention upon purchase. However, this issue appears to be largely redundant because, as discussed in Part II(B)(3), such transactions will typically be considered to be an enterprise for GST purposes because they constitute 'an adventure or concern in the nature of trade'.

3 *'In the Form of an Adventure or Concern in the Nature of Trade'*

If the activity or series of activities is not in the form of a business, as required by s 9-20(1)(a), there may still be an enterprise under s 9-20 if the activity is 'in the form of an adventure or concern in the nature of trade'.[58]

Whereas the notion of a 'business' (as previously discussed) is very familiar in Australian taxation law, the addition of the phrase 'an adventure or concern in the nature of trade' is not widely used nor is it defined in the *GSTA*.[59] It is also of interest to note that the Explanatory Memorandum to the Bill does not add any guidance on why this phrase was included in the definition of 'enterprise'.[60] Importantly, the

55 *Casimaty* (1997) 151 ALR 242, 261–2.

56 *Miscellaneous Taxation Ruling MT 2006/1* [277]–[283].

57 Ibid [291]–[307].

58 *ABNA* s 9-20(1)(b).

59 Hill, above n 14.

60 Explanatory Memorandum, A New Tax System (Goods and Services Tax) Bill 1998 (Cth) 7–8 [2.2]–[2.5].

Australian Taxation Office is of the view that the words 'in the form of' do not broaden which activities fall under this limb of the definition of an 'enterprise'.[61]

Given the lack of direct Australian statutory and judicial guidance on the precise meaning of 'adventure or concern in the nature of trade', it is desirable to examine other sources to assist in deriving the meaning of the term. The discussion below of these sources indicates that this phrase tends to capture one-off developments that fall short of constituting a business but involve property which was purchased with an intention to profit from reselling the developed properties. The importance of an intention to profit in this definition is reinforced by the specific requirement in s 9-20(2)(c) of a reasonable expectation of a profit or gain being needed to satisfy the definition of 'enterprise' if the taxpayer is an individual or a partnership.[62]

The words 'adventure or concern in the nature of trade' are used in the UK legislation,[63] and the Great Britain *Royal Commission on the Taxation of Profits and Income: Final Report*[64] provides a useful starting point in ascertaining the meaning of this term. This report established six badges of trade which comprise: the subject-matter of the realisation, the length of the period of ownership, the frequency or number of similar transactions by the same person, supplementary work on or in connection with the property realised, the circumstances that were responsible for the realisation and motive.[65] Notably, there is considerable accord between these six badges of trade and the indicia of a business used by the Australian courts, which suggests there could be considerable overlap between ss 9-20(1)(b) and 9-20(1)(a). Although these UK badges of trade have not been formally incorporated into the Australian tax legislation, they have been referred to in *Puzey* v *Federal Commissioner of Taxation* as factors that can be used to determine whether a taxpayer is carrying on a business.[66] Also in *Federal Commissioner of Taxation v Williams*[67] and *Swansea*,[68] 'business' and 'an adventure or concern in the nature of trade' are regularly used synonymously, and in neither case was any distinction made between the two concepts. Nevertheless, statutory interpretation rules require that the words and phrases used in legislation are taken as necessary and that a particular word or phrase does not render another meaningless or redundant.[69] The Australian Taxation Office is also of the opinion that the inclusion of this phrase

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61 *Miscellaneous Taxation Ruling MT 2006/1* [242].

62 *GSTA* s 9-20(2)(c).

63 *Income and Corporation Taxes Act 1988* (UK) c 1, s 832(1), sch D.

64 Great Britain, *Royal Commission on the Taxation of Profits and Income, Royal Commission on the Taxation of Profits and Income: Final Report (1955).*

65 Ibid 39–40 [116].

66 (2003) 131 FCR 244, 257 [48].

67 (1972) 127 CLR 226 ('*Williams*').

68 (2009) 72 ATR 120.

69 See, eg, *Commonwealth v Baume* (1905) 2 CLR 405, 414 (Griffith, CJ); *Project Blue Sky Inc v Australian Broadcasting Authority* (1998) 194 CLR 355 (McHugh, Gummow, Kirby and Hayne JJ).

indicates that the legislature intended to extend the meaning of an enterprise, and that it includes activities that do not meet the definition of a business because they lack continuity and repetition.[70]

The dictionary definition of 'trade' can also be used to assist in determining the meaning of 'adventure or concern in the nature of trade'. This is because interpretation principles require that an undefined term is applied using its common meaning and, to this end, courts have referred to dictionary definitions to assist.[71] The term 'trade' is defined in the *Macquarie Dictionary* as 'the buying and selling, or exchanging, of commodities, either by wholesale or by retail … a form of occupation pursued as a business or calling, as for a livelihood or profit.'[72] In addition, the *Oxford English Dictionary* defines it as a '[p]assage or resort for the purpose of commerce; hence, the buying and selling or exchange of commodities for profit'.[73] Both of these definitions emphasise the dealing of a commodity in the purchase and the sale aspects of the transaction, and also the expectation of profit. If it were undertaken on a regular and continuous basis the previous discussion would support the view that it would also be in the form of a business, therefore making it unnecessary to consider whether it is an adventure or concern in the nature of trade. On the other hand, as discussed previously, it is less likely that an isolated business deal or trade will be found to be a business.[74] While isolated developments are less likely to constitute a business, the dictionary definitions referred to support the conclusion that isolated developments that involve the purchase of property with an intention to profit through development and sale, constitute 'an adventure or concern in the nature of trade'.

Miscellaneous Taxation Ruling MT 2006/1 implies the Australian Taxation Office's view is that 'an adventure or concern in the nature of trade' has strong similarity to the term 'profit-making undertaking or scheme'.[75] The term 'profit-making undertaking or scheme' is used in a substantial amount of Australian case law.[76] However, while these notions are both aimed at one-off transactions,[77] there is no case law that

70 *Miscellaneous Taxation Ruling MT 2006/1* [244].

71 See, eg, *State Chamber of Commerce and Industry v Commonwealth* (1987) 163 CLR 329, 348 (Mason CJ, Wilson, Dawson, Toohey and Gaudron JJ); *Manly Council v Malouf* (2004) 61 NSWLR 394, 396–7 (Handley JA).

72 C Yallop et al (eds), *Macquarie Dictionary* (Macquarie Library, 4th ed, 2005) 1491.

73 Oxford University Press, *Oxford English Dictionary* (2015) <http://www.oed.com/>.

74 *Casimaty* (1997) 151 ALR 242; *Westfield Ltd v Federal Commissioner of Taxation* (1991) 28 FCR 333.

75 *Miscellaneous Taxation Ruling MT 2006/1* [233]–[238], [263]–[270].

76 The previous *Income Tax Assessment Act 1936* (Cth) s 26(a) made gains from a 'profit-making undertaking or scheme' assessable. This was subsequently re-enacted in *Income Tax Assessment Act 1936* (Cth) s 25A and later as *ITAA97* s 15-15 where the legislation refers to a 'profit-making undertaking or plan'.

77 In *AB v Federal Commissioner of Taxation* (1997) 37 ATR 225, 242, Foster J agreed with the comment that an adventure in the nature of trade is an isolated business venture as opposed to a continuing business.

directly suggests or implies that there is any overlap between them.[78] If in the future it is found that these concepts are strongly connected, then the substantial amount of Australian case law on profit-making undertaking or schemes would provide further guidance as to when a gain is an adventure or concern in the nature of trade. However, even this guidance would be limited, given that the courts have never decided that a gain is a profit-making undertaking or scheme while, at the same time, stating that the taxpayer is not running a business. Rather, in previous cases where it has been held that a gain is a profit-making undertaking or scheme, the courts either did not address the issue of whether there was a business or found that the gain was a result of both a profit-making undertaking or scheme and a business.[79]

The best indication of how Australian courts would interpret an adventure in the nature of trade is likely to be in accordance with the meaning of the term given by English cases relating to the buying and selling of assets, and how those cases have been interpreted by Australian courts. The collective English and Australian case law indicates that the phrase covers one-off developments that involve making a profit from property, which was purchased with an intention to profit from reselling the developed properties. At first, an English House of Lords decision held that an isolated commercial transaction that realised a profit from reselling an asset that had been purchased with an intention to resell did not constitute an adventure in the nature of trade.[80] A few decades later, however, another English House of Lords case found that it did.[81] In Australia, the High Court is of the view that the latter case effectively over-rode the first:

> Some twenty-five years after *Jones v Leeming* the Treasurer was vindicated, substantially if not entirely, by the House of Lords' decision in *Edwards (Inspector of Taxes) v Bairstow* … The irony of this is that the facts of *Jones v Leeming* are not readily distinguishable from *Edwards v Bairstow*…[82]

The importance of an intention to profit by resale when purchasing an asset, in deciding if the taxpayer is undertaking an adventure in the nature of trade, was illustrated in the UK case of *Marson (Inspector of Taxes) v Morton*.[83] In that case, the taxpayers had purchased property with an intention to hold the property long-term, but shortly after sold the property in its original state. Sir Nicolas Browne-Wilkinson VC of the Chancery Division held that the tribunal had not erred in its finding that the taxpayers had not undertaken an adventure in the nature of trade. Importantly, Sir Nicolas Browne-Wilkinson VC stated that the taxpayers' intention when purchasing the

78 In *McClelland v Federal Commissioner of Taxation* (1970) 120 CLR 487, 491, when referring to an 'adventure or concern in the nature of trade', the Privy Council stated that 'there is no similar provision in the Australian Act'.

79 Hanegbi, above n 29, 259.

80 *Jones v Leeming* [1930] AC 415 ('*Jones*').

81 *Edwards* [1956] AC 14.

82 *Whitfords Beach* (1982) 150 CLR 355, 376 (citations omitted).

83 [1986] 1 WLR 1343.

property was important to his finding.[84] Although case law indicates that in some circumstances it is possible for a taxpayer who sells an asset they originally acquired with an intention to profit through sale to not be regarded as carrying on an adventure in the nature of trade,[85] but rather as an investment activity,[86] this is unlikely to be the case for a property developer given that the development is an active endeavour rather than a passive investment.[87]

Subsequent High Court authority reinforces the view that the term 'an adventure in the nature of trade' typically covers small-scale developments by taxpayers who have an intention to resell upon purchase. Such authority appears to indicate that 'an adventure in the nature of trade' is very similar to the Australian tax concept of what is known as the 'first strand of *Myer*'. The first strand of *Myer* makes certain commercial transactions entered into with a profit intention fall into the income tax net.[88] The similarity of the two concepts is apparent in the judgment of *Myer*, where the High Court said, after discussing the abovementioned House of Lord cases of *Jones* and *Edwards* (which dealt with the issue of whether selling an asset that had been acquired for resale purposes constitutes an adventure in the nature of trade):

> The judgments in some of the English decisions naturally reflect the language of the United Kingdom statutory provisions, which have no precise counterpart in this country. However, over the years this Court, as well as the Privy Council, has accepted that profits derived in a business operation or commercial transaction carrying out any profit-making scheme are income, whereas the proceeds of a mere realization or change of investment or from an enhancement of capital are not income …
>
> It is one thing if the decision to sell an asset is taken after its acquisition, there having been no intention or purpose at the time of acquisition of acquiring for the purpose of profit-making by sale. Then, if the asset be not a revenue asset on other grounds, the profit made is capital because it proceeds from a mere realization. But it is quite another thing if the decision to sell is taken by way of implementation of an intention or purpose, existing at the time of acquisition, of profit-making by sale, at least in the context of carrying on a business or carrying out a business operation or commercial transaction.[89]

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84 Ibid 1348–9.

85 Ibid.

86 See, eg, *Manzur v Revenue and Customs Commissioners* [2010] UKFTT 580 (17 November 2010) where a retired surgeon who regularly bought and sold shares with an intention to profit from them was found by the First-tier Tribunal to be undertaking an investment activity rather than an adventure in the nature of trade.

87 *Marson (Inspector of Taxes) v Morton* [1986] 1 WLR 1343 emphasised that a transaction that involves some type of development or work on the subject matter is more likely to constitute an adventure in the nature of trade than one that does not: at 1348.

88 *Federal Commissioner of Taxation v The Myer Emporium Ltd* (1987) 163 CLR 199 ('*Myer*').

89 Ibid 212–13.

Specifically, the first strand of *Myer* applies where a taxpayer has undertaken a commercial or business transaction with the intention to profit from the transaction,[90] and subsequently realises the profit as intended.[91] In the case of a transaction that involves a resale, this means that the profit-making intention must be present at the time the asset is acquired.[92] Judicial decisions suggest that this principle is applicable even where the initial intention was not the sole or dominant one.[93] Furthermore, it will also apply where the taxpayer intended to profit in one of a few possible ways,[94] or where there was an intervening event that led to the property being unexpectedly used for private purposes and an accompanying delay in the sale.[95] Where the taxpayer is a company, the purpose of those who control it — typically its shareholders and directors — is relevant to establishing whether there was an intention to profit through sale at the time of purchase.[96] Although case law has not given a clear meaning as to what is meant by the requirement of a 'commercial transaction', judicial authority suggests that it is something that can fall short of constituting a business.[97]

Given the apparent similarities between the concepts of an adventure in the nature of trade and the first strand of *Myer*, it is worthwhile examining how Australian courts have applied the first strand of *Myer* to small-scale developers. The single judge Federal Court decision of *McCurry*[98] applied the first strand of *Myer* to hold that a one-off property development was not a business but was a commercial deal and, therefore, was ordinary income for income tax purposes. In *McCurry* the taxpayers purchased land that had an existing house on it which was of no value. They then proceeded to demolish the old house and constructed three townhouses on the land. The first attempt to sell the properties failed, but they were later sold at a profit after

90 Ibid 209–10. However, it should be noted that the *Myer* decision is open to interpretation: see P Burgess et al, *Cooper, Krever & Vann's Income Taxation: Commentary and Materials* (Thomson Reuters, 7th ed, 2012) 305 [5.380]: '[m]any learned minds have attempted to plumb the depths of the *Myer* judgment. You also may care to try to comprehend exactly what was being said.'

91 *Myer* (1987) 163 CLR 199, 213.

92 Ibid.

93 *Federal Commissioner of Taxation v Cooling* (1990) 22 FCR 42. Although this case did not involve property development, the Court discussed it in the context of the overriding principle regarding a transaction entered into with a profit-making motive.

94 *Westfield Ltd v Federal Commissioner of Taxation* (1991) 28 FCR 333, 344.

95 *McCurry v Federal Commissioner of Taxation* (1998) 39 ATR 121 ('*McCurry*').

96 *Ruhamah Property Co Ltd v Federal Commissioner of Taxation* (1928) 41 CLR 148 in deciding whether a gain was assessable under a specific provision that assessed profit-making schemes. The case was cited with approval and applied in *Whitfords Beach* (1982) 150 CLR 355, 370 (Mason J) in deciding whether a business was present. The principle was also applied in *Antlers Pty Ltd v Federal Commissioner of Taxation* (1997) 35 ATR 64 in deciding whether the gain was assessable under a specific provision that assessed profit-making schemes.

97 *McCurry* (1998) 39 ATR 121, 124–5.

98 Ibid 124–8.

a short period when the properties were used by the taxpayers and their family as their private residence. Central to Davies J's decision was the application of the *Myer* principle to the facts in this case, which indicated that the taxpayers, although not conducting a business, undertook a commercial dealing and had acquired property with the intention of developing it and then selling it at a profit.[99]

In addition to the case law that indicates the connection between an adventure in the nature of trade and the first strand of *Myer*, there is some limited Australian case law that directly discusses what an adventure in the nature of trade is, in the context of deciding whether gains are ordinary income for income tax purposes. The comments in these cases are consistent with an adventure in the nature of trade generally being fulfilled where the taxpayer has resold property that was purchased with an intention to resell. Conversely, they indicate that a lack of intention to profit by resale upon purchase will generally mean that there is no adventure in the nature of trade. The Australian Taxation Office is of the view that a simple subdivision of land will constitute an adventure in the nature of trade if the land was purchased with the intention of profiting by subdividing and sale.[100]

In the first of these cases, the High Court in *Williams*[101] considered, in part, whether the sale of land was an 'adventure in the nature of trade' in relation to deciding if the sale of property was assessable as ordinary income. In *Williams*, the High Court was concerned with the sale of land that had originally been purchased with an intention to later sell at a profit, but had instead been gifted to Mrs Williams (the spouse of the person who purchased the property) and later sold by Mrs Williams. In holding that the sale was not an adventure in the nature of trade, the Court placed emphasis on whether Mrs Williams had a profit intention at the time of acquiring the property.[102] This was seen as a critical factor in determining whether there was an adventure in the nature of trade.

In *McClelland v Federal Commissioner of Taxation*[103] the taxpayer, together with her brother, had inherited a large tract of land as co-owners. The brother wished to sell his interest. However, as the taxpayer did not want to co-own the land with a stranger, she offered to buy her brother's interest. To pay for the purchase from the brother, the taxpayer sold a portion of the land just after acquiring the brother's interest. One of the issues was whether the profit on the sale of land pertaining to the interest acquired from her brother was ordinary income due to the taxpayer undertaking an adventure in the nature of trade. The Privy Council reversed the High Court's decision and, by majority, found that there was no adventure in the nature of trade. Specifically, the majority appeared to base its decision on the fact that the taxpayer's intention was to keep the land, but practical circumstances made her embark upon

99 Ibid 124–6.

100 *Miscellaneous Taxation Ruling MT 2006/1* [242].

101 (1972) 127 CLR 226.

102 Ibid 231–3 (Stephen J), 248–50 (Gibbs J).

103 (1970) 120 CLR 487.

the sale.[104] The majority distinguished the English case of *Iswera v Inland Revenue Commissioners*[105] that had held there was an adventure in the nature of trade as the taxpayer there had purchased land with an intention to subdivide and sell, and then carried out that intention.[106]

In the single judge High Court decision of *Eisner v Federal Commissioner of Taxation*[107] the taxpayer purchased two properties. The Court accepted that they had been purchased by the taxpayer with the intention of building apartments on them and subsequently renting them out. The taxpayer had borrowed money for this purchase from one of the companies that he controlled. However, as the taxpayer was unable to obtain the requisite finance for development, he chose to incorporate a new company and sold the properties to this company at a substantial profit. Another company controlled by the shareholder then built units for sale on the land. One of the issues that the Court had to consider was whether the gain was ordinary income. In deciding that the gain was not an adventure in the nature of trade, Walsh J was swayed by the fact that the properties had been purchased for the purpose of developing and renting them out.[108] His Honour mentioned that although the taxpayer had sold the property by incorporating a company that bought the property at a high price, this did not mean that the gain was ordinary income due to it being an adventure in the nature of trade.[109]

From the decisions in *Williams*, *McLelland* and *Eisner* there is support for the view that an adventure in the nature of trade requires at the point of purchase an intention to profit through sale. In these cases it was held that the taxpayers were not engaged in an adventure in the nature of trade because their original intention was to profit from the use of the property rather than from its sale.

It, therefore, is reasonable to conclude that if a small-scale developer can be shown to acquire the property with an intention to develop and sell at a profit, and acts out this intention, then the activity is highly likely to be an adventure in the nature of trade, even though it is not necessarily an activity in the form of a business. This is consistent with the view of the Australian Taxation Office that property purchased with an intention to resell at a profit will mean that the activities constitute an 'enterprise'.[110] However, where property was originally purchased without an intention to resell it for profit, but is then subsequently developed and sold in a manner that falls

[104] Ibid 495–7.

[105] [1965] 1 WLR 663.

[106] *Williams* (1972) 127 CLR 226, 397.

[107] (1971) 45 ALJR 110.

[108] Ibid 113–14.

[109] Ibid 114–15.

[110] *Miscellaneous Taxation Ruling MT 2006/1* [270]–[276]. Examples 28 and 29 indicate that the Australian Taxation Office also believes that the sale of property that was purchased with an intention to develop and sell constitutes an adventure in the nature of trade.

short of constituting a business, the judicial evidence appears to indicate that it would not constitute an adventure in the nature of trade. However, in this second situation, if the taxpayer proceeds to develop the property extensively it would seem, depending on the individual circumstances, that they are potentially undertaking a business.

C *Registration Threshold*

Although anyone who is carrying on an enterprise is allowed to register for GST,[111] registration is compulsory where the taxpayer is carrying on an enterprise and (unless it is a non-profit body) their turnover for GST purposes exceeds the turnover threshold of $75 000.[112]

The effect of the legislation is that the relevant information for determining whether registration is required is the taxpayer's projected GST turnover.[113] Projected GST turnover at any given point is the sum of the 'values'[114] of supplies made or likely to be made in the current month and the next 11 months.[115] However, it is very important to note that sales of capital assets are not counted in determining the projected GST turnover of an enterprise.[116] Consequently, for small-scale property developers, the value of supplies included in their projected GST turnover will be the sum of the 'values' of non-capital property sales in the current month and the projected sales in the next 11 months.

As nearly all properties sold by a small-scale developer would be materially over $75 000, the developers carrying on an enterprise would need to register, at the latest, just after the first sale of a developed property.[117] However, if the properties are regarded as capital the threshold would not be breached and registration would not be required.

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111 *GSTA* s 23-10.

112 Ibid ss 23-5, 23-15; *A New Tax System (Goods and Services Tax) Regulations 1999* (Cth) reg 23-15.01. The turnover threshold for a non-profit body is $150 000; however, this article does not deal with non-profit bodies.

113 *GSTA* s 188-10(1) states that the turnover requirement will be met when the current GST turnover is at least $75 000 and the Commissioner is not satisfied that the projected GST turnover is below $75 000, or the projected GST turnover is at or above the turnover threshold. The net effect of this provision is that the projected GST turnover will ultimately decide whether the registration threshold has been met.

114 Ibid s 9-75. 'Value' is defined in the *GSTA* as the pre-GST amount, which is calculated as 10/11 of the GST inclusive sale 'price': at s 9-75(1).

115 Ibid s 188-20. Excluded are input taxed supplies, supplies that are not for consideration and not covered by s 72-5 and supplies that are not connected with the enterprise carried on.

116 Ibid s 188-25.

117 Part III of this article will examine the optimal time that a taxpayer should register.

Example

> Alex is a small-scale developer who bought a large house, demolished it and built three townhouses on the property. He sold each of the townhouses for $400 000. The first is sold on 5 February 2014, the second on 20 December 2014 and the third on 5 March 2015. On the assumption that Alex is carrying on an enterprise, registration for GST would be required during February 2014 because, at that point, the projected GST turnover would be over $75 000, given that the turnover would include sales made in February 2014 through to January 2015.

1 *Registration is Not Required When Properties are Regarded as Capital*

As previously stated, the relevant registration threshold does not include payments that the *GSTA* regards as capital.[118] Thus, if a small-scale developer's properties are regarded as part of capital, it is unlikely there will be a turnover of at least $75 000, meaning that there is no need to register for GST and so any GST liability will be avoided. This will generally only be an issue if the taxpayer has developed the properties for rental purposes and then subsequently sold them.

A preliminary issue is whether the sale of properties by landlords will typically be considered as being in the course or furtherance of an enterprise, which, as discussed, is one of the requirements for GST registration.[119] Although this paper has earlier discussed when a small-scale developer's activities are in the course of furtherance of an enterprise, unique issues arise when the taxpayer sells the properties that were developed for rental purposes.

A landlord will be carrying on an enterprise because the definition of enterprise includes activities undertaken 'on a regular or continuous basis, in the form of a lease, licence or other grant of an interest in property'.[120] However, it is arguable that if this is the only means by which they are carrying on an enterprise, the sale of those properties could not be considered to be undertaken in the course or furtherance of that leasing enterprise. Consequently, an issue arises as to whether developing properties for rental, renting them out and then selling them could be carrying on an enterprise under one of the other limbs of the definition of 'enterprise'. If it is, there is a much stronger argument that the sale of the properties could be considered to be in the course of that enterprise.

It would be very unlikely for a taxpayer who develops property for rental or private purposes to be regarded as carrying on an enterprise by carrying on an adventure in the nature of trade. This is because the 'badges of trade', described earlier in this paper, are unlikely to be fulfilled when a development involves building properties for the sole purpose of earning rental income. Specifically, the subject matter of realisation, the length of period of ownership, the motive and that rental properties

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118 *GSTA* s 188-25.

119 Ibid s 9-5(b).

120 Ibid s 9-20(1)(c).

are investment assets[121] are badges which, in the case of a rental development, would make it very unlikely that an adventure in the nature of trade has been undertaken.[122] Although this issue has not been directly addressed in Australia, there is English authority supporting the proposition that developing a property for the purpose of rental is not an adventure in the nature of trade.[123]

However, a taxpayer's activities that involve building properties for rental could, in some circumstances, be regarded as a business and, consequently, be regarded as an enterprise for GST purposes.[124] If this is the case, then the final act of selling these properties could be considered part of this enterprise. As discussed earlier in this paper, some isolated land developments undertaken by small-scale developers to sell the developed land could also constitute the carrying on of a business, even where the land was not purchased with the intention to sell. This depends, however, on a number of factors including the size and extensiveness of development. It therefore follows that in some situations developments that are undertaken with the intention to rent out the properties upon completion could also constitute a business. Whether such a taxpayer would be considered as carrying on a business depends on the extent to which they fulfil the indicia of a business mentioned earlier in this article. Alternatively, it is possible, though unlikely, that the act of renting out properties, regardless of the preceding development, is of itself regarded as a business. Where the rental activities are a business, and so an enterprise for GST purposes, there is a strong argument that the final act of selling the properties would be included as part of that enterprise. Though a normal small-scale landlord who purchased and rented out a pre-existing investment property

121 Australian Taxation Office, *Goods and Services Tax: New Residential Premises and Adjustments for Changes in Extent of Creditable Purpose*, GSTR 2009/4, 24 June 2009, [41]–[43] ('*GSTR 2009/4*') considers operations that develop properties for rental, and indicates that such properties are capital and that they are 'investment assets'.

122 The alternate view is that although developing a property for rental would be an activity that lacks some of the badges of trade, it could still be an adventure in the nature of trade because the word 'trade' is broadly defined as including the provision of goods or services: *Re Ku-ring-gai Co-operative Building Society (No 12) Ltd* (1978) 36 FLR 134, 139.

123 In *Simmons (Liquidator of Lionel Simmons Properties) v Inland Revenue Commissioners* [1980] 2 All ER 798 the House of Lords found that a company that had purchased and developed properties for the purpose of rental, but had been forced to liquidate them, was not undertaking an adventure in the nature of trade regarding those properties.

124 In *Lilydale Pastoral Co Pty Ltd v Federal Commissioner of Taxation* (1987) 15 FCR 19, 26, Pincus J stated that purchasing property to rent out fulfilled the relevant definition of 'enterprise' because it was an 'undertaking of a business or commercial kind.' However, the relevant definition of 'enterprise' in that case was 'a business or other industrial or commercial undertaking' (*Income Tax Assessment Act 1936* (Cth) s 128A(1)) and so differed from the definition of 'enterprise' that is in the GST legislation. It cannot be said with certainty that Pincus J regarded the taxpayer as carrying on a business given that he regarded the activities as a 'business or commercial kind'.

would be unlikely to be carrying on a business,[125] there is English authority that states that if the taxpayer is in a corporate form, then renting out properties is much more likely to constitute a business than would otherwise be the case.[126]

Consequently, it would appear that a taxpayer who has developed properties with the purpose of renting those properties, but subsequently changes their mind, could be carrying on an enterprise because they are carrying on a business. The result is that the sale of the properties could be regarded as occurring in the course of that enterprise. In this scenario, the next issue to consider is whether such properties would be considered capital, meaning that the taxpayer need not register for GST, having not reached the registration threshold.

Although the word 'capital' has been considered at length in the context of the income tax legislation, there is no judicial authority as to its meaning within the GST legislation. Consequently, use could reasonably be made of the income tax interpretation of its meaning.[127] Although a thorough examination of the definition of the term 'capital' is beyond the scope of this article,[128] in the modern income taxation law context, capital expenditures are those that are related to the business structure, whereas revenue (non-capital) expenditures are regarded as relating to the process of earning income.[129] Although this judicial test is far from decisive, an expense is more likely to be capital if the expenditure is not recurring, results in the creation of long-lasting assets and is a one-off payment.[130]

Despite the fact that Australian courts have not directly addressed the issue of whether rental properties are capital, it is implicit in some tax decisions that they are.[131]

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125 *Federal Commissioner of Taxation v McDonald* (1987) 15 FCR 172.

126 *American Leaf Blending Co Sdn Bhd v Director General of Inland Revenue* [1979] AC 676, 684, though Diplock J did state that '[i]n the case of a private individual it may well be that the mere receipt of rents from property that he owns raises no presumption that he is carrying on a business.'

127 See, eg, *Ramaciotti v Federal Commissioner of Taxation* (1920) 29 CLR 49, 53 (Knox CJ).

128 The history and background of Australian tests for ascertaining if an expense is capital can be found in Burgess et al, above n 90, 487–91 [9.20]–[9.40].

129 *Sun Newspapers Ltd v Federal Commissioner of Taxation* (1938) 61 CLR 337, 359 ('*Sun Newspapers*').

130 Ibid 362.

131 See *Federal Commissioner of Taxation v Hyteco Hiring Pty Ltd* (1992) 39 FCR 502 ('*Hyteco*'); *Federal Commissioner of Taxation v Cyclone Scaffolding Pty Ltd* (1987) 18 FCR 183 where it was held that proceeds of sale of rental goods were capital. Although the Courts did not explicitly state that the goods were capital, it follows that the findings that the sale proceeds were capital for income tax purposes were at least partially based on the leased goods being capital. For instance, in *Hyteco* (1992) 39 FCR 502, 511 the Court implied that the leased goods were capital by stating '[w]hat the present case is concerned with is a profit arising on a sale to third parties of the very apparatus with which the taxpayer conducted its business, not a profit

GSTR 2009/4 also suggests that such properties would be regarded as capital.[132] Consequently, a taxpayer need not register for GST if they develop properties with the intention of renting them out, and without an intention to sell them, but then subsequently sell them due to changing their mind. This will be the case even if the sale is regarded as being in the course of an enterprise, because the sale will be capital in nature and capital items are not included in the calculation of the registration threshold. Furthermore, a taxpayer who builds properties with the intention of renting those properties but has the long-term intention to sell them at an indefinite point in time, but then changes their mind and sells them in a more immediate time horizon, might also be regarded as being in the same position.[133] A taxpayer wishing to argue that their properties were capital to avoid GST registration would need to show evidence supporting the claim that their genuine intention when developing the properties was not to sell them.[134]

An unresolved issue concerns whether taxpayers who have mixed intentions when purchasing and developing properties are able to avoid GST registration by claiming

from the process by which the taxpayer operated to obtain regular returns by means of regular outlays', followed by a reference to *Sun Newspapers* on deciding if an expenditure is capital: at 511 [36]. Although the cases of *Memorex Pty Ltd v Federal Commissioner of Taxation* (1987) 77 ALR 299 and *Federal Commissioner of Taxation v GKN Kwikform Services Pty Ltd* (1991) 91 ATC 4336 involved businesses whose disposal of rental goods were found to be income rather than capital, their judgments were based on the facts of those cases, in that the sales of goods were sufficiently regular and expected (traits of gains that have an income character for tax purposes) rather than based on a denial that the goods were capital. Furthermore, inherent in McKerracher J's reasoning in *Swansea* (2009) 72 ATR 120, 141, in accepting that a taxpayer that held assets as long-term investments was carrying on an enterprise, was that those long-term assets were regarded as capital. See also *GSTR 2009/4* [41]–[43], which discusses an operation that develops properties for rental, and says that such properties are capital, and that they are 'investment assets'.

132 *GSTR 2009/4* [42]–[43].

133 See *GXCX v Federal Commissioner of Taxation* (2009) 73 ATR 380 in which the Administrative Appeals Tribunal ('AAT') held that for the purposes of the relevant GST provisions, an intention to rent accompanied with an intention to sell in the long-term at an indefinite point in time was regarded as equivalent to a sole intention to rent. The relevant GST provisions were those that allowed the taxpayer to claim the GST component for costs used to develop properties built for sale, but not for costs used to develop properties for rent. It can be arguably extrapolated that the same logic applies in determining whether properties are capital, in that properties built for rent with a long-term view of selling them at an indefinite point are treated the same as properties solely built for rent and so are regarded as capital.

134 See *Abeles v Federal Commissioner of Taxation* (1991) 22 ATR 504; *Crow* (1988) 19 ATR 1565; *McCurry* (1998) 39 ATR 121 for cases where the taxpayers' claimed intention upon purchasing their land was met with scepticism by the Court. In *McCurry*, Davies J said that '[i]n a case such as this, where the Court must examine the purpose of a transaction, the court is entitled to have regard not only to the evidence which the taxpayers give of what they had in mind but also to the surrounding facts and to the events which actually occurred': at 127.

that the properties are capital. It appears that a developer who originally intends only to rent the properties, or intends to rent them out and sell them at an indefinite time many years later, can claim that they are capital. The position is less certain, however, in circumstances where a taxpayer purchases and develops properties with an intention to both rent them and subsequently sell them at a definitive point in the short or medium term. When, if ever, would such a taxpayer with mixed purposes be able to claim that their properties are capital? While the income tax legislation, in denying a deduction for capital expenditures, allows a partial denial for expenditures that are partially capital,[135] the *GSTA* does not allow partially capital goods to be partially counted or not counted in determining the GST registration threshold.[136]

III Consequences of Registration

If it is ascertained that GST registration is required, the next step is to gain an appreciation of how to calculate the amount of GST payable.

A *GST Liability*

In general, GST will be payable on the selling price of the real estate (calculated as 1/11 of the selling price) for taxpayers who are registered or are required to register for GST.[137] While most sales of residential property do not attract a GST liability (even for GST registered taxpayers)[138] this exclusion does not apply to sales of new residential premises.[139] Residential premises that are sold for the first time, as well as premises that have been built to replace demolished premises, are both regarded as new residential premises.[140] Consequently, small-scale developers required to register for GST will incur a GST liability upon selling their property. While it is true that substantially renovating a building can also change its legal status to a new residential premises,[141] the nature and extent to which one can renovate an existing building and not be caught under such an exclusion is outside the scope of this article.

135 In *ITAA97* s 8-1(2) the effect of the words ‘to the extent that’ is that a taxpayer is partially denied a deduction for expenditures that are partially capital in nature.

136 *GSTA* s 188-25 refers to disregarding the counting of ‘transfer of ownership of a capital asset of yours’.

137 Ibid ss 9-70, 9-75.

138 Ibid s 40-65(1).

139 Ibid s 40-65(2)(b).

140 Ibid s 40-75. For a discussion regarding the current case law as it applies to this exemption, see John Tretola, Sylvia Villios and Pasqualina Callea, ‘GST and Residential Premises —Which Intention is Relevant?’ (2011) 21 *Revenue Law Journal* 69; Robin Woellner, ‘Wherever You Hang Your Hat May be Home, but is it “Residential Premises” for GST Purposes?’ (2010) 3 *Journal of the Australasian Law Teachers Association* 139; Sylvia Villios, ‘Australian GST and Residential Property — Uncertainty Abounds’ (2010) 6 *International VAT Monitor* 423.

141 *GSTA* s 40-75(1)(b).

However, if a new residence has been used as a rental property for at least five years, its subsequent sale will not be subject to GST.[142] In practice, this rule would appear, to some extent, to be redundant. This is because, as discussed earlier in this paper, properties that are built for the purpose of earning rental income are typically not counted in determining the GST threshold when subsequently sold. This is the case even if the sales are regarded as being in the course of an enterprise, as the properties are capital and so the registration threshold will not have been reached. However, a taxpayer who is able to use this five-year statutory rule has the advantage that they need not face any of the evidentiary issues that might concern a taxpayer claiming that the properties are capital.[143]

B *Entitlement to Input Credits*

1 *Introduction to Input Credits*

A developer will typically not be entitled to an input credit for the cost of the residential property that was subsequently developed.[144] However, a taxpayer liable to pay GST for the sale of their developed properties is also entitled to claim input credits; GST input credits, by their nature, lower GST liability.[145] Taxpayers will generally be entitled to claim as input credits the GST portion of costs incurred to develop the properties,[146] which will be equal to 1/11 of the amount they paid for such costs.[147] Examples of costs that would typically have GST in the price would be the price of contract labour and materials. If those costs are incurred in the same tax period as the sale of the properties, the input credits can be used to reduce the GST liability from the sale of the properties.[148] If they are incurred in an earlier tax period, then they will lead to an entitlement to get a refund from the Australian Taxation Office.[149] The tax period for small-scale developers will typically consist of four quarters of three months each.[150] However, for the taxpayer to be entitled to an input credit for such costs they must be registered for GST at the time those costs arose.[151]

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142 Ibid s 40-75(2).

143 As discussed earlier in this paper, a taxpayer claiming that their properties are capital will need evidence that they were originally built with the intention of renting.

144 *GSTA* ss 11-5, 9-5, 40-65. However, if the property used for development was a new residential property, or vacant land, and the seller was registered for GST, and GST was included in the price, then an input credit would be available for the GST registered developer.

145 Ibid ss 7-5, 7-15, 17-5.

146 Ibid s 11-20.

147 Ibid ss 11-25, 9-70, 9-75.

148 Ibid ss 7-5, 7-15, 17-5.

149 Ibid s 7-15.

150 Ibid s 27-5.

151 Ibid s 23-10.

2 *When Should the Taxpayer Register?*

Developers carrying on an enterprise will usually be required to register for GST just after the sales contract for the developed property has been entered into. Such a taxpayer may choose to register earlier,[152] but whether they should do so depends on the facts. For instance, if a taxpayer in this situation acquires property on or after 1 July 2000, they ideally should register for GST prior to incurring costs of developing their property.[153] Where the development involves the purchase of vacant land on or after 1 July 2000, then if the vacant land's sale subjects the seller to a GST liability, the purchaser's registration should occur before purchasing the land.[154] Registering for GST at this earlier stage will allow the purchaser to claim input credits on their costs. If the purchaser does not register for GST prior to incurring costs there is scope for them to request retrospective GST registration.[155]

Where retrospective GST registration is requested, the Commissioner of Taxation is able to agree to such a request for those carrying on an enterprise.[156] However, the Commission of Taxation is only able to backdate the registration for a maximum of four years.[157] Consequently, unregistered developers who will have to register for their sale but who have not been able to claim input tax credits on costs that have GST included, have a four-year window to backdate registration to enable them to claim the input tax credits. On the other hand, due to the operation of the margin scheme (discussed in Part III(C)), a taxpayer who acquired their property prior to 1 July 2000 should ideally register for GST only at the time when they have to, which is right after the sales contract of their developed properties has been entered into. If they have several properties to sell they should register after entering into the first sales contract. Although such a taxpayer will not be able to claim input credits for the costs of construction, the operation of the margin scheme will ensure no GST liability arises from the sales.[158]

3 *Entitlement to Input Credits Where Property is Acquired for Mixed Purposes*

An issue may arise as to the extent to which input credits can be claimed for a GST registered developer who exhibits more than one purpose. This will be the case where the development was undertaken for both the purposes of sale and

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152 Ibid s 23-10.

153 Ibid s 29-10. The precise point at which a relevant cost could potentially lead to an input credit if the taxpayer is registered will depend on whether they account on a cash basis or not.

154 As mentioned in this case, an input credit could normally be claimed on the land.

155 *GSTA* s 25-10(1)(b)(i).

156 Ibid.

157 Ibid s 25-10(1A).

158 This principle is explained in more detail in the next part of this paper.

rental.[159] In this case, the extent to which a registered developer would be able to claim the input credits will depend on the circumstances. For example, a taxpayer who initially entered into the development with the sole intention of sale would be able to claim full input credits for their relevant costs,[160] whereas a taxpayer who entered into a development with the mixed purposes of first renting out the developed properties and then selling them would only be allowed to claim a fair and reasonable pro-rata portion of the input credit.[161] The matter becomes even more complex if the registered developer originally had one intention upon development, but then subsequently changed their mind. In this situation, the developer would be required to make a subsequent GST adjustment to reflect the change of circumstances.[162] For instance, a taxpayer that originally intended to sell the properties upon development, but then changed their mind and first rents out the developed properties prior to sale, will have to pay back a proportion of their input credits by way of adjustment.[163] Conversely, a taxpayer who started developing properties with the intention of renting them out and then selling the developed properties, but then ends up only selling the properties can, by way of adjustment, claim further input credits.[164]

A taxpayer who develops properties with the genuine intention of renting the properties and without the requisite intention to sell, but then ends up selling them, will, as discussed in this paper, generally not be required to register for GST because the GST registration threshold will not have been reached. However, if for some reason this developer chooses to register for GST they would not be allowed to claim input credits during the development stage,[165] even though the sale would be subject to GST.[166] Due to their change of purpose, they could, however, make subsequent

159 In *Commissioner of Inland Revenue v Morris* (1997) 18 NZTC 13 385, 13 393 Giles J (referring to s 21(1) of the *Goods and Services Tax Act 1985* (NZ)) said that 'there is nothing inconsistent or illogical about two different but contemporaneous purposes.'

160 *GSTA* ss 11-5, 11-15. This is assuming that the taxpayer did not change their mind once the property had been developed.

161 Ibid s 11-30; *GSTR 2009/4* [25].

162 *GSTA* div 129; *GSTR 2009/4* [67]–[68]. A GST adjustment under div 129 changes the entitlement to an input credit for an acquisition.

163 *GSTA* div 129; *GSTR 2009/4* [54]–[57]. An AAT decision has found that if a taxpayer intends to sell their properties, ends up renting them, but continues to have a long-term, indefinite plan to sell them if possible, they will have to make the same adjustment as if they had no long-term indefinite plan to sell the properties: *GXCX v Federal Commissioner of Taxation* (2009) 73 ATR 380. Logically, this means that a taxpayer who purchases and develops a property with the intention to rent, but has a long-term plan to sell the properties at an indefinite time, will be in the same position as a taxpayer who builds and develops a property with an intention to rent but has no such intention to sell.

164 *GSTA* div 129.

165 Ibid ss 11-15, 40-65.

166 Ibid s 9-5 as it would then fulfill all the requirements of a 'taxable supply'.

adjustments to claim some input credits,[167] but as the sale would be subject to GST, they would have an overall GST liability.

C *Margin Schemes*

A taxpayer incurring a GST liability upon sale can normally claim input credits on most of their building costs (as long as they are registered at that time), but in most cases they will not be able to claim an input credit for the original property acquisition costs. This is because one of the requirements of entitlement to an input credit is that the acquisition has GST included in the price.[168] As discussed, the sale of residential real estate will not (except if considered new) trigger a GST liability, meaning that the purchaser will not be entitled to an input credit even if they are registered for GST. There are some exceptions, however, such as when the small-scale developer purchases vacant land (which, by its nature, is not considered a residential premises) from a party that is registered for GST.

However, *GSTA* div 75 does, in essence, offer a notional input credit to taxpayers not entitled to an input credit on their property purchase. The way it does this is by what this division refers to as the 'margin scheme'.

1 *Operation of the Scheme*

Specifically, the legislation states that where the margin scheme applies, the GST liability will not be based on 1/11 of the sales price, but rather on 1/11 of the margin between the sales price and the following:[169]

i) If the property was acquired on or after 1 July 2000, then the acquisition cost of the property.[170] This does not include costs such as stamp duty and legal fees.[171]

ii) If, however, the taxpayer acquired the property prior to 1 July 2000 and was registered for GST as at 1 July 2000, the relevant value is the value of the property as at 1 July 2000. This will include the value of any improvements made to the land which are present as at 1 July 2000.[172]

iii) If the taxpayer acquired the property prior to 1 July 2000, but only became registered or required to be registered for GST after 1 July 2000, the relevant value is when GST registration was made.[173]

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167 Ibid div 129.

168 Ibid s 11-5.

169 Ibid s 75-5.

170 Ibid s 75-10(2).

171 Australian Taxation Office, *Goods and Services Tax: The Margin Scheme for Supplies of Real Property Acquired on or After 1 July 2000*, GSTR 2006/8, 26 April 2006, [49].

172 *GSTA* s 75-10(3) items 1, 3.

173 Ibid s 75-10(3) item 2.

In the latter two of these three cases, a valuation will have to be made of the property but this valuation can be made after the relevant date.[174] For instance, if the relevant value of the property is at 1 July 2000, the valuation can still be made at a later date as long as the valuation pertains to the relevant date. Furthermore, the taxpayer will have a choice as to how to make the valuation based on the following three methods:[175]

i) A valuation by an approved valuer.

ii) The consideration received by the supplier under the contract of sale. However, this second valuation method, as explained below, can only be used in specific circumstances.

iii) As determined before the valuation date by relevant State or Territory Government for rating or land tax purposes.

The operation of the margin scheme will mean that the taxpayer will, in substance, at the time of sale, receive an input credit of 1/11 of the relevant cost or value of the land. Furthermore, the relevant cost or value of the land will not include any costs that the taxpayer has claimed input credits on.[176] This is because if the property was acquired on or after 1 July 2000, then for the margin scheme, the cost of the property at acquisition is relevant so it could not include any costs on which input credits have been claimed. If the property was acquired before 1 July 2000, then for the margin scheme, the relevant value will be the value of the land at the later of when GST registration was made or 1 July 2000, which means that no input credits could have been claimed for the relevant valuation time.[177]

2 *Further Details on the Second Valuation Method*

The second valuation method — the consideration received under the sales contract — can only be used when the sales contract has been entered into prior to the relevant valuation date (the date at which the property's value is relevant for the

[174] Australian Taxation Office, *Goods and Services Tax: How the Margin Scheme Applies to a Supply of Real Property Made on or After 1 December 2005 that was Acquired or Held Before 1 July 2000*, GSTR 2006/7, 26 April 2006, [61].

[175] Australian Taxation Office, *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination*, MSV 2009/1, 14 October 2009.

[176] In *Sterling Guardian Pty Ltd v Federal Commissioner of Taxation* (2006) 149 FCR 255, the Full Federal Court held that where the relevant value was the consideration paid by the purchaser, the consideration did not include any costs of improvement made after the land was acquired. The legislature has reinforced this finding in *GSTA* s 75-14.

[177] If the relevant valuation time was 1 July 2000, then no input credits could have been claimed before this date as this is the date on which the GST came into effect. If the relevant valuation time is when the taxpayer registered for GST, then no input credits could have been claimed before then as registration is required.

margin scheme).[178] The valuation date, as discussed, is only an issue for property purchased before 1 July 2000, and will generally be the later of 1 July 2000 or when the taxpayer is registered for GST. Thus, in practical terms, this method will generally only be an option if the property was purchased prior to 1 July 2000 and GST registration was made after the contract for sale was entered into.

Utilising this valuation method is highly advantageous to the taxpayer as it will result in no GST liability for the sale in question.[179] This is because this method values the property at the sales price, meaning that the taxable margin, being the difference between the sales price and relevant property value (valued at sales price), is nil. Consequently, a small-scale developer who acquired the property prior to 1 July 2000 and has to register should hold off registering until just after the sales contract has been entered into.

Example

> Simone purchases an established house and land during July 1998 for $150 000. Upon purchase she intended to rent the house out for a few years, demolish it, build three townhouses and sell them. On 1 July 2000 the property is valued at $250 000. During July 2011 Simone starts developing the property. She has it valued at $650 000 at that time just before the development commenced. She registers for GST at that time because she knows that when she sells the townhouses she will be required to pay GST and so wishes to claim input credits on the relevant expenses. She then spends $33 000 on demolishing the house and $660 000 building three townhouses. She could claim an input credit for 1/11 of these costs, which would mean that these credits are worth $63 000 in total. She subsequently sells the townhouses for $750 000 each. Due to the margin scheme, her GST liability will be reduced by the relevant value of the property. This means that upon sale, her GST liability would be [(750 000 × 3) – 650 000] × 1/11 = $145 456, and when the input credits of $63 000 are taken into account, the amount of GST payable in net terms on the development would be $82 456.
>
> A better strategy in this case would have been for Simone not to register for GST until the time the townhouses were to be sold. Although this would preclude her from claiming input credits for the development costs, it would also mean that the value for the margin scheme would be the sales price of $750 000. As a result, the GST liability would be based on 1/11 of the difference between the sales price and relevant value, which would be [(750 000 × 3) – (750 000 × 3)] × 1/11 = 0.

178 Australian Taxation Office, *Goods and Services Tax: How the Margin Scheme Applies to a Supply of Real Property Made on or After 1 December 2005 That was Acquired or Held Before 1 July 2000*, GSTR 2006/7, 26 April 2006, [80B].

179 *GSTA* ss 75-5, 75-10.

3 *Apportionment*

A development that includes subdividing a property or developing it into stratum units will typically result in several different sales. If the sales are made in different tax periods, and the relevant value for the margin scheme is the consideration of the property paid by the taxpayer, the consideration needs to be apportioned against the portions of the divided property in a fair and reasonable manner.[180] For instance, property purchased in 2008 for $1 million and subsequently subdivided and developed by building two townhouses that are of equal size and value would result in each of the sales being offset with $500 000 of the property's purchase price.

4 *Buyer's Consent*

One condition of the margin scheme is that both the seller and purchaser must consent in writing to its application.[181] That is, a small-scale developer wishing to utilise the margin scheme must get the purchaser's consent to use the scheme. The reason why the purchaser's consent is required is because the legislation disallows the purchaser from claiming an input credit, even if registered. However, in practice, a private person purchasing from a small-scale developer would be indifferent to being barred from claiming input credits on their property purchase because they are not likely to be registered for GST. Even if the purchaser is registered, living in the property, renting it out[182] or selling it,[183] these are typically not activities for which one can claim an input credit, even without it being specifically prohibited by the laws relating to the margin scheme.

IV Conclusion

Whether a small-scale developer's sales are subject to GST can have a substantial impact on the profitability of their development. However, for many such developers determining whether there will be such a liability will not be easy, given the considerable uncertainty in some aspects of the law.

Central to this uncertainty is the definition of enterprise in s 9-20(1) of the *GSTA* and its critical elements of

> an activity, or series of activities, done:
>
> (a) in the form of a *business; or
>
> (b) in the form of an adventure or concern in the nature of trade …[184]

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180 Ibid s 75-15; Australian Taxation Office, *Goods and Services Tax: The Margin Scheme for Supplies of Real Property Acquired on or After 1 July 2000*, GSTR 2006/8, 26 April 2006, [58]–[68] suggests some fair and reasonable apportionment methods.

181 *GSTA* s 75-5(1)(c).

182 Ibid ss 11-15, 40-35.

183 Ibid ss 11-15, 40-65.

184 Ibid s 9-20(1)(a)–(b).

Consideration of these elements is critical in determining whether a small-scale development project could be subject to GST.

In relation to the definition of business the authors suggest that where the activities are on a small scale and are infrequent, then the extent of the development and whether the taxpayer is directly involved in the project will be important in determining whether there is an enterprise for GST purposes. The taxpayer's GST liability therefore ultimately depends on the individual facts. The post-*Whitfords Beach* cases indicate that there would be many instances where there is a marked degree of doubt about whether or not a small-scale developer is carrying on a business.

Where the activity is held not to be a business it may still be an enterprise where it is in the form of an adventure or concern in the nature of trade, but in Australia this aspect of the definition has only received limited judicial guidance. The authors, however, believe that it is reasonable to conclude that if a small-scale developer can be shown to acquire the property with an intention to develop and sell at a profit, and acts out this intention, then the activity is likely to be an adventure or concern in the nature of trade even if it is not a business. Conversely, if there is no such initial intention then the matter is likely to be resolved by whether or not the extent of the subsequent work carried out in the development constitutes a business in itself.

Importantly, small-scale developers whose sales are potentially subject to GST need to have a good knowledge of the operation of the GST provisions regarding input credits and the margin scheme, or in the alternative utilise an adviser that has such expertise. Such expertise is critical for minimising GST liability which can potentially diminish a material portion of their profit. Specifically, the timing of GST registration can have an impact on the developer's tax burden.

Despite these uncertainties, taxpayers and professionals with a sound understanding of the relevant law discussed in this article will be much better placed to determine whether any given small-scale development's sale will result in a GST liability.