

Analysis of the Bill

- 2.1 The only stakeholder to raise concerns about the Bill was the Institute of Chartered Accountants in Australia (ICAA). The ICAA's submission covered the amendments of the GST treatment of hire purchase (Schedule 3(3)) and the reversal of the Full Federal Court decision in *Gloxinia Investments*. These issues are discussed below.

Schedule 3(3) – the GST treatment of hire purchase

Background

- 2.2 Division 156 of the *A New Tax System (Goods and Services Tax) Act 1999* covers supplies and acquisitions made on a progressive or periodic basis. This currently covers hire purchase arrangements. Section 156-25 provides that the Division does not apply if a taxpayer accounts on a cash basis.
- 2.3 The Bill seeks to insert section 156-23 into the Act, stating that Division 156 does not apply to hire purchase. It also seeks to insert Division 158 to specifically cover hire purchase, stating that taxpayers who account on a cash basis are treated as not accounting on a cash basis for the purposes of the Act and regulations for these agreements. The implication is that cash accounting taxpayers will be able to obtain input tax credits up front from the interaction of this new Division with other provisions in the tax law.
- 2.4 However, the ICAA expressed concern about the provisions because they implement the policy intent through other provisions in the tax law, rather than by explicit statement.¹ For example, the ATO has issued a ruling of its interpretation of the general attribution rules that a taxpayer who accounts

1 Mr Michael Evans, ICAA, *Committee Hansard*, Canberra, 16 December 2011, pp. 4, 9.

for GST on an accruals basis can claim input tax credits up front for hire purchase.² However, the Institute has stated that this interpretation is open to question:

... there seems to be a doubt, just on the basis of the law that we have, as to whether this is the supply of credit as well as the supply of goods, in which case there would be two supplies being made for different prices. In the institute's view, the operation of the general rule about when the GST on those two supplies is payable is open to question. It depends when the part of the consideration is paid for each of the parts of the supplies.³

- 2.5 The Institute also raised the question of how GST for hire purchase would interact with the luxury car tax, in particular whether the GST-inclusive price of the supply of credit would inadvertently increase the value of a car for the purposes of luxury car tax:

When we get to the luxury car tax and the credit limitation issue we have to work out for the purpose of luxury car tax, and for the limitation on input tax credits for luxury cars, what the price of the car is. It takes us back to the question of whether this is a supply or two supplies. Without something clear in the law to say that, it seems to me, as a matter of the legal form of a contract, the price of the car is the 60 monthly payments, including the interest component, which would mean the luxury car tax could be higher.⁴

- 2.6 As the Institute noted in the hearing, this depends on whether hire purchase is treated as one or two supplies, in the former case a supply of goods by way of hire, or in the latter case a supply of goods and a supply of credit. Although this relates to the regulations, rather than the Bill, it warrants discussion due to the coverage it received in the hearing and its relevance to the GST treatment of hire purchase generally.

Analysis

- 2.7 In response to the Institute's position that the interpretation of the GST law in relation to hire purchase is uncertain, Treasury responded that the ATO is satisfied with its approach. Treasury also stated that the sorts of

2 ATO, *Goods and Services Tax Ruling, Goods and services tax: attributing GST payable, input tax credits and adjustments and particular attribution rules made under section 29-25*, GSTR 2000/29, 11 July 2007, para. 211.

3 Mr Michael Evans, ICAA, *Committee Hansard*, Canberra, 16 December 2011, p. 3.

4 Mr Michael Evans, ICAA, *Committee Hansard*, Canberra, 16 December 2011, pp. 4-5.

changes that the Institute have been canvassing are wide ranging, yet the industry feedback in the Treasury's *Review of the GST financial supply provisions* favoured refinement over fundamental reform. Further, the bodies representing the hire purchase and equipment leasing industries fully support the provisions at an operational level:

... the sorts of changes that Mr Evans is seeking probably go to the fundamental core of our GST, and the government is probably not in a position to have a complete, wholesale revision of our existing GST law. I do not think it is simply a matter of a couple of words in the legislation to deal with that issue.

Secondly, my advice is: the commissioner is comfortable administering the law as it is. He believes he has the necessary backing, in the combination of the legislation and the regulations, to deal with his existing interpretation and, as I said, to date that has not been challenged in the courts. As I have said before, the other people at the operational level, who are issuing and dealing with taxpayers and providing hire purchase agreements, fully support the legislation as it currently stands.⁵

- 2.8 Treasury's comment that the amendments have industry support were corroborated by the industry itself. The Australian Finance Council and the Australian Equipment Lessors Association stated in their submission:

The equipment finance industry was delighted when in the 2010-11 Budget the Government announced its intention to amend the financial supply provisions of the GST law, allowing full input tax credits upfront for businesses accounting on a cash basis when they enter into hire purchase arrangements ...

This is a significant tax reform measure. It will address the adverse consequences of the current tax treatment of hire purchase, which has created a tax inefficiency which has driven taxpayers to other finance products. As such, this amendment enhances the integrity of Australia's GST regime.⁶

- 2.9 In relation to the question of whether there will be one or two supplies under hire purchase and whether the supply of credit would increase the value of a car for the luxury car tax, Treasury stated in evidence that this was a matter for the regulations, in particular that:

5 Mr Rob Dalla-Costa, Treasury, *Committee Hansard*, Canberra, 16 December 2011, p. 5.

6 Australian Finance Conference and the Australian Equipment Lessors Association, *Submission 3*, pp. 1-2.

... we will attempt to address some of the uncertainty that the ICAA are raising in the context of the regulations, where we can give more emphasis to the separate supply nature of the provisions.⁷

- 2.10 On 13 January 2012, the Government released exposure draft regulations amending the *A New Tax System (Goods and Services Tax) Amendment Regulations 2012*. Items 2 and 3 in the draft regulations provide that hire purchase arrangements will not be financial supplies, so both components of a hire purchase transaction will be fully taxable and administratively easier for operators.⁸ Making hire purchase transactions fully taxable for GST does not increase the tax burden for operators because the transactions are business to business and they receive input tax credits for the amounts involved. In relation to the luxury car tax, the Explanatory Memorandum to the draft regulations features an example of how the new provisions will operate. It states that the GST-inclusive price of the supply of the car is not included in calculations for the luxury car tax.⁹

Conclusion

- 2.11 The committee is confident that the Bill will deliver its policy intent in relation to hire purchase. The ATO has taken the view that its interpretation of the GST for hire purchase is supported by the legislation and there has been no court challenge to date on this point. Further, the recently released Explanatory Memorandum on the draft regulations make clear that there will be no inadvertent consequences with the luxury car tax. Schedule 3(3) can proceed as drafted.

Schedule 4: GST on new residential premises

Background

- 2.12 ICAA expressed its support for the overall intention of the amendments, which was to restore the general state of the law following the outcome of the *Gloxinia Investment* case. However, ICAA qualified this support by setting out several reservations. Firstly, ICAA was concerned by the Bill's

7 Mr Rob Dalla-Costa, Treasury, *Committee Hansard*, Canberra, 16 December 2011, p. 6.

8 Mr Rob Dalla-Costa, Treasury, *Committee Hansard*, Canberra, 16 December 2011, p. 3.

9 A New Tax System (Goods and Services Tax) Amendment Regulations 2012, *Explanatory Memorandum*, p. [4].

very specific focus. In their submission, they referred to the fact that previous amendments to the GST have tended to be narrowly prescriptive and required subsequent amendment.¹⁰ In the ICAA's own words at the hearing:

Our view comes from an acceptance of the stated policy and the policy reiterated in *Gloxinia* that the sale of newly constructed premises should be subject to full GST when they go into consumption. We accept that it appears that the proposed response to the deficiency highlighted in *Gloxinia* only addresses the *Gloxinia* situation, yet it is still stated that the policy intention is that newly constructed residential premises will be subject to full tax. If the policy is that that will only apply in the circumstances of *Gloxinia*, then we could have no complaint with these amendments.¹¹

- 2.13 Secondly, the ICAA were concerned that the Explanatory Memorandum of the Bill had introduced other matters that would also have broader implications for the administration of the law. In particular the Explanatory Memorandum stated that the treatment of barter transactions between developers and Crown agencies granting long-term leases would be taxable and creditable (for example, in infrastructure projects). This had not been announced in the press release of 27 January 2011.¹² The ICAA advised the committee that the treatment of 'barter transaction within the Explanatory Memorandum is inconsistent with the way the commissioner had administered law until he withdrew the law in 2008 and was not a matter that was addressed in the press release of 27 January'.¹³

Analysis

- 2.14 In their testimony before the committee, the Treasury advised that schedule 4 of the Bill was solely intended to address the specific facts of *Gloxinia Investments*.¹⁴ They acknowledged that the circumstances in the *Gloxinia Investment* case were only one example where the GST may not be applicable. They also acknowledged that the amendments in the Bill might not necessarily address a range of other circumstances where GST should be applied in line with the policy intent. Treasury representatives explained their position as follows:

10 ICAA, *Submission 1*, p. 4.

11 Mr Michael Evans, ICAA, *Committee Hansard*, Canberra, 16 December 2011, p. 12.

12 Mr Michael Evans, ICAA, *Committee Hansard*, Canberra, 16 December 2011, p. 12.

13 Mr Michael Evans, ICAA, *Committee Hansard*, Canberra, 16 December 2011, p. 12.

14 Mr Phil Bignell, Treasury, *Committee Hansard*, Canberra, 16 December 2011, pp. 5, 12.

The purpose of the amendments is to restore the intended policy outcome concerning new residential premises that arises from the decision of the full Federal Court in *Gloxinia* ... We believe that they are fairly widely supported by stakeholders in the form that they have been contained ... Treasury considered a broader principled change in response to the *Gloxinia* decision. We put that out for public consultation in the Treasury discussion paper released earlier in the year. Most submissions did not support the broader approach that the institute has proposed ... Treasury did not feel satisfied that the wider approach would address the issue without having a wider change of policy and potential revenue implications.¹⁵

2.15 In relation to barter supply and projects sponsored by Crown agencies, Treasury explained that the treatment of barter transactions had been carefully considered, following liaison with the Property Council of Australia. The inclusion of barter transactions in the Explanatory Memorandum was intended to ensure the clarity regarding the implications of the amendment for such transactions.¹⁶

2.16 Treasury also acknowledged that there was a risk that the Bill might not prevent future litigation, but this needed to be understood within the correct context. The GST remains a new tax compared with older taxes such as the income tax. Therefore the law is less settled and litigation does occur. As Treasury advised the Committee at the hearing:

The GST is a relatively new law, having been in place for 11 years, compared with our income tax, which has been a much more settled system. In recent years we have had many cases coming before the courts to test that new law, so it is certainly possible that there will be additional matters that will arise in the future with new areas of the law. Those certainly cannot be ruled out.¹⁷

Conclusion

2.17 The committee expects that Schedule 4 will ensure that taxpayers in the same circumstances as in *Gloxinia Investments* will pay GST on new residential premises in line with the policy intent. The proposal in the Bill has been subject to thorough consultation. The alternative proposed by ICAA, namely more fundamental reform, was rejected by stakeholders

15 Mr Phil Bignell, Treasury, *Committee Hansard*, Canberra, 16 December 2011, p. 12.

16 Mr Phil Bignell, Treasury, *Committee Hansard*, Canberra, 16 December 2011, p. 12.

17 Mr Phil Bignell, Treasury, *Committee Hansard*, Canberra, 16 December 2011, p. 14.

and potentially had wider revenue implications. The Bill contains a practical solution and it has the committee's support.

Overall conclusion

- 2.18 The Bill has a number of components, some of which received express endorsement in submissions. The provisions on the electronic portability form create a system whereby super fund members will be able to electronically request the consolidation of their super through the ATO. This will assist individuals who are reunited with their superannuation funds in consolidating the different amounts.
- 2.19 Many of the provisions for CGT and business restructures are beneficial to taxpayers. For example, under current law, taxpayers can obtain a CGT roll-over for a capital gain or loss that arises from their interest in a company or trust because of the demerger of an entity from the group of which the company or trust is the head entity. However, this is not available where the head entity is a corporation sole or complying superannuation entity. Schedule 2(2) of the Bill makes this roll-over available for these types of bodies.
- 2.20 The GST and hire purchase amendments remove a tax-induced distortion between chattel mortgage and hire purchase. Under current law, chattel mortgage is more attractive because the GST input tax credits are up front for small businesses that use cash accounting for GST, whereas they are only available on a payment basis under hire purchase. Small businesses now rarely use hire purchase for this reason, despite its other advantages over chattel mortgage.
- 2.21 The Bill also reduces compliance costs for small business by increasing the financial acquisitions threshold from \$50,000 to \$150,000. If a small business makes financial acquisitions below this amount, then it is outside the financial supply regime and can claim input tax credits for its financial supplies. Increasing this threshold takes more small businesses outside the financial supply regime and allows more businesses to claim input tax credits on their financial supplies.
- 2.22 The amendments for GST and new residential premises will reverse the effect of the court case *Gloxinia Investments*, which found that, where a particular combination of strata titles and leases were involved, newly constructed residential premises were not subject to GST. The Bill will re-affirm the policy intent that newly constructed homes should be subject to

GST. They will also protect the revenue that funds Government services that assist the whole community. The Bill overall comprises measures that are important refinements to the tax system.

- 2.23 The ICAA was the only stakeholder to raise concerns about the Bill. These were the provisions to enable businesses acquiring assets through hire purchase to obtain their GST input tax credits up front and the provisions to reverse the effect of the recent court decision of *Gloxinia Investments*. The ICAA's concerns related to whether the provisions would implement the policy intent, rather than the policy itself.
- 2.24 Despite the ICAA's comments, there are several reasons why the provisions in the Bill are the best available solution. For example, in relation to hire purchase, the ATO believes it has sufficient legislative basis for its interpretation and there have been no court actions disputing them. Further, in consultations in the review of GST and financial supply, stakeholders rejected the more fundamental reforms of the GST implied by ICAA's submission. Finally, the equipment finance industry itself is 'delighted' with the proposal.
- 2.25 In relation to GST for new residential premises, the ICAA has again suggested a wider reform than that supported in consultations. Treasury has noted that there is a risk of further court action in this area if the Bill proceeds, but this is part of bedding down what is still a relatively new tax. After scrutinising Treasury and the ICAA, and noting the many positive measures in the Bill, the committee is of the view that it should proceed unamended.

Recommendation 1

- 2.26 **That the House pass the Tax Laws Amendment (2011 Measures No. 9) Bill 2011 as proposed.**

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Chair
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