# RESIDENTIAL PROPERTY, COMMERCIAL PROPERTY, GOODS AND SERVICES TAX AND DEREGISTRATION: A CASE STUDY ON HOW THE GST LAW MAY HAVE BEEN MANIPULATED.

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**ABSTRACT**

When a residential property, being used for commercial purposes is sold to a buyer that intends to operate a professional practice from the premises and one of the vendors is registered for GST, what happens when the registered vendor deregisters from GST ten days before settlement? The purchaser expects to be able to claim the GST included in the price as an input tax credit but on settlement is not given a tax invoice. The purchaser then lodges the Business Activity Statement (BAS) claiming an input tax credit without a tax invoice. The purchaser believed that the Commissioner of Taxation would exercise his discretion under s 29-70(2) or under s 29-10(10) of the A New Tax System (Goods and Services Tax) Act 1999 (Cth), (GST Act) and treat the contract for sale as a tax invoice. The justification for this action being that the vendor deregistered from GST in order to retain the GST. In the case study presented in this paper the Commissioner of Taxation disallowed the purchasers' claim for the input tax credit. The main question examined in this paper is whether it is within the spirit of the GST legislation for a vendor to deregister just before settlement, not provide a tax invoice and keep the GST?

## I INTRODUCTION

It is not the intention of this paper be critical of the administration of the GST legislation by the Australian Taxation Office (ATO). It is also not possible to identify the actual vendors and purchaser in this transaction without impugning their character. The paper is intended to assist both the ATO and prospective purchasers of

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real property as to a potential problem where the vendor deregisters for GST in order to collect the extra 10 percent of the price and the purchaser is not provided with a tax invoice. It is not being suggested in this paper that the ATO is failing in its obligations under the legislation to protect both the revenue and innocent taxpayers from the potential for abuse by vendors that deregister for GST. In this situation only one of the joint vendors was registered for GST although it was assumed that the business that was conducted from the premises was as a partnership. Moreover, the purchaser did not specifically address the question of GST and whether or not the price included GST. The contract of sale indicated that the price did not include GST but the purchaser did not question the vendors as to the correct treatment. Nor did the vendors give an assurance that the purchaser would be able to claim an input tax credit. There were mistakes made on the part of the purchaser and possibly the vendors.

The paper will commence with a description of the circumstances that led to the purchaser being denied the input tax credit on the purchase of a residential property to be used for business purposes. This will involve an examination of the GST status of the vendors at the time the contract was signed and their GST status at the date of settlement.

Part II of the paper will examine the application of GST to real property, both residential and commercial as well as the concept of a 'going concern'. This part of the paper will also examine the ability of the Commissioner of Taxation to overcome the situation where a tax invoice has not been issued but should have been. This will also cover the way in which the Commissioner's discretion should be exercised to allow an input tax credit to be claimed based on Practice Statement LA 2004/11.

Part III of the paper will discuss the current situation where it would appear that GST may be avoided simply through the act of deregistering just prior to settlement. Finally a conclusion will be drawn as to whether this particular tactic by a vendor is within the spirit of the law and can be used for that purpose in light of the fact that it would be expected that taxpayers signing the declaration when deregistering are not deliberately trying to avoid paying GST.

## A The Fact of the Case Study

The property was located in the outer suburbs of Melbourne and consisted of a former residential home that had been used by the vendors for commercial purposes. The purchaser intended to use the former residential property for the purpose of conducting an accounting and financial planning practice. The purchaser had an Australian Business Number (ABN) and was registered for GST. The vendors were husband and wife but only the husband was registered for GST as they conducted a business from the premises. There is no information as to whether the husband and wife conducted the business as a partnership or as a sole trader. There is no information as to whether the business paid rent to both the husband and wife as joint owners of the property and GST was included in the commercial rent. The further issue of joint tenancy as opposed to tenants in common is not dealt with in this paper

but it may be relevant for the purposes of determining whether the husband could legally dispose of 50 percent of the property as a taxable supply. All of this information would help to clarify the GST status of the vendors. The vendors and purchaser entered into a contract of sale on 29 July 2010 with settlement due on 29 October 2010.

The contract price was $400,000. The standard Real Estate Institute of Victoria contract for the sale of real estate was used by the parties to the transaction. This contract was in the form prescribed by the *Estate Agents (Contracts) Regulations 2008* (Vic). Clause 13 covers GST and at paragraph 13.1 it states the following:

> The purchaser does not have to pay the vendor any GST payable by the vendor in respect of a taxable supply made under this contract in addition to the price unless the particulars of sale specify that the price is plus GST. However, the purchaser must pay to the vendor any GST payable by the vendor:
> (a) solely as a result of any action taken or intended to be taken by the purchaser after the day of sale, including a change of use; or
> (b) if the particulars of sale specify that the supply made under this contract is a farming business and the supply does not satisfy the requirements of section 38-480 of the GST Act; or
> (c) if the particulars of sale specify that the supply made under this contract is a going concern and the supply does not satisfy the requirements of section 38-325 of the GST Act[1]

The real property in question was not farming land; it was not the sale of a going concern; and the use to which it was currently being used was not to change. The special treatment of farming land and going concerns will be discussed briefly in the next part of the paper. The contract was specifically marked as the price not including GST. The specific box needed to have the words 'plus GST' inserted in it in order for the purchaser being required to pay $400,000 plus GST of $40,000. In this case the words 'plus GST' was not inserted into the contract for sale. The contract specifically excluded reference to farming land and to the margin scheme applying. The margin scheme will be discussed briefly in the next part of this paper. On the face of it, the contract indicated that the price of $400,000 did not include GST. Again this was because there was no specific reference to the price of $400,000 plus GST. However, the purchaser did not clarify this issue with the vendors prior to signing the contract.

On settlement the balance of the purchase price, namely $360,000 was paid given that a deposit of $40,000 was paid at the date of the contract. The vendors did not provide the purchaser with a tax invoice but the purchaser had intended to claim the sum of $36,363 as an input tax credit.[2] Unbeknown to the purchaser, the only vendor being registered for GST, namely the husband had 10 days earlier deregistered for GST. The wife, having not been registered for GST at any time earlier, was not involved directly with the deregistration process. The vendor, in this case the husband, applied to deregister himself retrospectively effective from 30 June 2010. In effect, the vendor

[1] Real Estate Institute of Victoria, Contract of Sale of Real Estate, Form 1 – particulars of sale, Clause 13.
[2] This represents 1/11th of the purchase price being 10 percent of the value.

was placed in the position to claim that he was not registered for GST when the contract was signed, namely on 29 July 2010. At no time during negotiations for the purchase did the purchaser question the vendors over their GST status and in hindsight this would have helped to clarify this matter. This situation highlights the fact that mistakes are more costly when involving real property and it is vital that vendors and purchasers are provided with very good advice before signing contracts.

The purchaser then lodged their BAS and claimed an input tax credit for the $36,363. The ATO denied the claim on the basis that no tax invoice had been issued by the vendors. Clearly the vendors were not in a position to provide a tax invoice as they had deregistered for GST. The ATO considered imposing penalties on the purchaser but in the end declined to take this action.

A number of issues are raised in this situation and each will be examined in the following part of this paper. The issues to be assessed can be summarised as follows:

(1) Was the sale of the commercial residential premises a 'taxable supply' and what are the consequences where one of the vendors is registered for GST and the purchaser is registered for GST?
(2) Did the purchaser have a legitimate expectation, based on the wording of the contract for sale, that they would legally be able to claim the GST as an input tax credit?
(3) Would the vendors or the husband only have been required to pay GST if they had not deregistered? The wife had not been registered for GST which may or may not raise additional questions.
(4) Was the process of deregistering 10 days before settlement legitimate and was this strategy used to prevent the purchaser from claiming an input tax credit and the vendors from paying GST?
(5) Should the Commissioner have exercised his discretion and allowed the purchaser to claim the input tax credit in the absence of a tax invoice and take action against the vendors for payment of the GST?

## II THE GST IMPLICATIONS

The vendors had been carrying on a business from the premises that they sold in accordance with s 9-20 of the GST Act. The business was in the nature of an enterprise. The property was being used for a creditable purpose within the meaning of s 11-15 of the GST Act in that they were carrying on an enterprise from those premises. The vendors would have obtained an ABN and if their turnover had been in excess of $75,000 they would have needed to be registered for GST, s 23-15. Similarly, the purchaser had an established financial planning and accounting practice and had been carrying on an enterprise within the meaning of s 9-20. The purchaser had an ABN and was registered for GST.

## A When should GST be included in the price of residential premises?

The main question to be answered within this context is was the sale of the real property a 'taxable supply' within the meaning of the GST Act? If so, were the vendors required to pay 10 per cent of the value or 1/11th of the price to the ATO as the GST due on the sale of property? The supply of the real property will either be a taxable supply; a GST free supply; or an input taxed supply. GST is only an issue in this case if the sale of the house and land was a taxable supply. Prior to reaching a conclusion on this point, it is necessary to examine the following situations where real property has a different GST treatment depending upon the use to which it is being put and the registration requirements of the vendor and purchaser.

### *1 Residential Premises*

Generally the sale of residential premises that are existing homes are input taxed supplies and not subject to GST, s 40-65, GST Act. This means that costs which include GST, involved in acquiring or selling the residential home are not capable of being claimed as an input tax credit. In most cases the vendor and the purchaser are not registered for GST simply because they are not disposing of the property in the course of a business.[3] Residential premises are considered to be land or a building that is actually occupied as a residence.[4] For the sale of the residential premises to be an input taxed supply, as opposed to a taxable supply, pursuant to s 40-65, they must satisfy the condition that they are 'used predominantly for residential accommodation'.[5]

This contention is supported by the Full Bench of the Federal Court in the case of *Marana Holdings Pty Ltd v Federal Commissioner of Taxation* (2004) 57 ATR 521, where it was held that the term 'residential' requires an aspect of permanency or long term occupation.[6] In this case a former motel that was converted to strata titled home units could not be said to have been residential premises when first acquired. Therefore the sales of the new strata titled apartments were 'new residential premises' and taxable supplies.[7] GST had to be included in the price or the margin scheme used for the purchasers. In the present situation, the real property had not been used by the vendors as residential premises as they conducted a business from the property. The purchaser did not intend to use the premises as a residential property and this was made known to the vendors.

The next question is: are the premises to be treated as 'commercial residential premises'? If this is the case then the sale of the real property is not an input taxed

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[3] Philip McCouat, *Australian Master GST Guide*, (9th ed. 2009) 275.
[4] Ibid.
[5] Ibid, 276. See also ATO GST Ruling GSTR 2000/20.
[6] (2004) 57 ATR 521, 527.
[7] Ibid, 535.

supply.[8] In order for the property to be treated in this way the premises must be used for accommodation and have the characteristics outlined in GST Ruling, GSTR 2000/20.[9] The Commissioner contends that the intention of the purchaser should be taken into account in determining whether the premises are commercial residential premises. At paragraph 83 he outlines a number of factors that should be taken into account such as the commercial intention of the taxpayer; multiple occupancy; holding out to the public; accommodation is the main purpose; central management; management offers accommodation in its own right; the services offered; and the status of guests.

The distinction between 'residential premises' and 'commercial residential premises' is an important one since a supply of 'commercial residential premises' by way of sale is potentially a taxable supply.[10] Commercial residential premises are a subset of residential premises.[11] However, the definition of 'commercial residential premises raises a number of issues in its interpretation. The definition is as follows: commercial residential premises means:

(a) hotel, motel, inn, hostel or boarding house; or

(b) premises used to provide accommodation in connection with a school; or

(c) a ship that is mainly let out on hire in the ordinary course of a business of letting ships out on hire; or

(d) a ship that is mainly used for entertainment or transport in the ordinary course of a business of providing ships for entertainment or transport; or

(e) a caravan park or a camping ground; or

(f) anything similar to residential premises described in paragraphs (a) to (e).

The most disappointing thing about the above definition is the 'just in case' subsection (f) which would render the definition useless.[12] It is the existence of this subsection that would lend weight to the argument that purchasers of strata titled units should be able to claim an input tax credit and that the Commissioner's ruling requiring 'multiple occupancy' is incorrect.[13] The subsection refers to 'anything similar' should be interpreted in light of the criteria (a) to (e).

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[8] Ibid, 280.
[9] Ibid, 281.
[10] Tony Van Der Westhuysen, 'Just What is a "Residence" for GST Purposes?', (2008) 3(1) *Journal of the Australasian Tax Teachers Association* 116 125.
[11] Ibid.
[12] Ibid.
[13] GST Ruling GSTR 2000/20 at paragraph 52 and Tony Van Der Westhuysen , 126.

Once again, this category of 'commercial residential premises' does not apply to the current situation examined in this paper. The premises which had originally been used for residential premises had been used in a commercial enterprise and were to be used in the future for a commercial enterprise by the purchaser.

*2 Going Concern*

Was the purchase of the real property part of the acquisition of a 'going concern'? The sale of a going concern, namely a continuing business enterprise, is a GST-free supply provided it satisfies the conditions set out in s 38-325, GST Act. In order to satisfy this section, the sale must be for consideration. In other words it must be for money or something of value, s 9-15. Next, the buyer must be registered for GST on and from the date of the sale.[14] A further requirement is that the seller and buyer must have agreed that the sale is of a going concern; the seller carries on the business right up until the date of settlement; and the seller supplies the buyer with all things necessary for the enterprise to continue to operate.[15] One of the issues of the case study that is not examined in this section is whether or not the husband and wife vendors were registered for GST in their tax law partnership. The purchaser did not discuss this issue with the vendors and only became aware that the husband was the only joint owner of the property that was originally registered for GST.

In the current situation it would be impossible to comply with this section. First, the business carried on by the vendor was not that of a financial planner and accounting practice. Second, the seller and buyer did not agree that it was the sale of a going concern, and third; the premises could not be said to be a necessary supply in order for the continued operation of the same business. Therefore the sale of the former residential premises was not a GST-free supply pursuant to the provisions of s 38-325, as a 'going concern'.

*3 Farming Land*

If farm land is sold as a going concern, it will also be a GST-free supply. However, even if farm land is not sold as a going concern, it will still be GST-free in certain circumstances. If a farming business has been conducted on the land for at least five years before sale it will be GST-free, s 38-480. The concession also applies to farm equipment and not only the land. In that situation the sae of farming equipment and land will be GST-free provided a farming business will continue to be conducted by the purchaser. In the current case study, the former residential premises were not sold as farming land and therefore it was not GST-free.

[14] Ibid, 310.
[15] Ibid.

*4 Margin Scheme*

The next issue to be determined is whether or not the margin scheme applied to this particular sale of real property? If the margin scheme applied then the purchaser would not be entitled to claim an input tax credit. In order for the margin scheme to apply the seller must be registered for GST. In the current situation the seller was registered but deregistered retrospectively so that they would not satisfy this condition. The sale must not be GST-free, as discussed above, or an input taxed supply.

The margin scheme basically provides relief for buyers who are not registered for GST and who wish to use the property as a residential home and not as part of an enterprise. The seller must be registered for GST and carrying on an enterprise. Moreover, the sale must not be GST-free or an input taxed supply. The margin scheme is typically applied by property dealers and developers selling to home buyers.[16] In that situation, the vendor only adds the 10 per cent GST to any increase in value of the property since 1 July 2000. If the property being sold was acquired after 1 July 2000, the margin scheme can also be used even if the vendor acquired the property as a GST-free supply because the vendor was not registered for GST, and input taxed supply, or from a vendor that used the margin scheme when selling the property.[17]

If the margin scheme is used this prevents the purchaser from claiming an input tax credit for the GST paid, and in this situation a tax invoice is not required to be issued, s 75-30. However, in the present case study neither the vendor nor the purchaser 'ticked the box' to indicate that the margin scheme was to apply to the transaction even though at the time the contract was signed the vendor was registered for GST.

The sale of real property that is used for commercial purposes, as an office from which an enterprise is to be conducted, would be a taxable supply and not a GST-free supply or an input taxed supply. That is the situation in this case study and the two issues that now remain to be examined are what is the effect of the deregistration process and should the Commissioner have exercised his discretion and allowed the claim for an input tax credit without a tax invoice being supplied by the vendor? More importantly, should there be in existence a process whereby deregistration is not accepted where a large transaction is yet to be settled. In this case the vendor was due to receive the sum of $400,000 from the sale of commercial premises.

*5 Sale of assets when enterprise ceases*

Another explanation for the justification by the vendor to deregister when still disposing of the assets of the enterprise is found in section 188-25, GST Act. Section

[16] Ibid, 288.
[17] S 75-5, GST Act.

188-25 allows for the sale of assets to be disregarded when considering the GST turnover figure if the supply is being made as a consequence of ceasing to carry on an enterprise or substantially reducing the size and scale of the enterprise. This allows the vendors to deregister and still dispose of assets connected with the former business. However, there is no evidence that the business that was conducted by the vendors from the premises in question was being reduced in size or even ceasing to operate. Clearly the main asset was being disposed of, but the business may have continued from other premises. If that was the case then the deregistration process should taken place.

## B Deregistration for GST – requirements

A taxpayer is required to cancel their registration within 21 days when they cease to carry on an enterprise, 25-50. However, if you are doing something in the course of terminating your business you are still considered to be carrying on an enterprise and you should maintain your registration.[18] In this case study, it could be argued that the vendor was still carrying on their enterprise by disposing of the assets of the enterprise. Of course, if the turnover drops below $75,000 then the registration can be cancelled even though the enterprise continues to operate.

The Commissioner can cancel the registration as at the date of the determination to cancel the registration or the taxpayer can request a retrospective cancellation, 25-60. The retrospective cancellation can only apply to a date at the start of a tax period, s25-65. In the current case study, the vendor was granted retrospective cancellation back to 30 June 2010 even though the contract to sell the real property was dated 29 July 2010. The application for cancellation was made by the vendor on 19 October 2010.

In order to obtain a retrospective cancellation, the taxpayer would be required to show the ATO that they have not held themselves out to other businesses as being registered for GST.[19] The taxpayer is required to sign a declaration to that effect. A false declaration can attract severe penalties. However, the purchaser contends that they were aware that the vendor was registered for GST at the time of signing the contract and they specifically told the vendor that they intended to use the real property for carrying on an enterprise. However, they did not advise the vendor that they intended to claim an input tax credit.

It would appear that deregistration is virtually automatic and that the ATO does not question taxpayers as to the accuracy of the form. Obviously the ATO relies on the fact that the taxpayer is making a declaration and that the contents are correct. It may be unrealistic for the ATO to devote resources to checking the accuracy of the information contained in the cancellation form and therefore taxpayers may be in a position to take advantage of the situation. In the present case study, it may have been

[18] Philip McCouat, n 2, 49.
[19] Ibid, 50.

expected that the vendor would apply for cancellation of their GST registration once all the assets of the vendor's enterprise had been disposed of in the normal course of terminating the enterprise. That was not the case being examined in this paper. This then leads to the final question: should the Commissioner have exercised his discretion in favour of the purchaser and accepted the contract of sale as being equivalent of a tax invoice pursuant to s 29-70(1), GST Act?

## C No Tax Invoice – Commissioner's discretion

In order for the Commissioner to exercise his discretion in this type of situation, the sale of the commercial premises must have been a taxable supply. In light of the above analysis, it is strongly contended that the supply of the premises were of a commercial nature and therefore a taxable supply. However, the deregistration of the vendor prior to the actual settlement of the real property may have rendered this a non-taxable supply but this issue would require further evidence from the vendors. It is also contended in this paper that the vendors failed to comply with subsection 29-70(2) of the GST Act which requires a party that makes a taxable supply to provide the recipient, in this case the purchaser, with a tax invoice for the supply within 28 days of the recipient requesting a tax invoice. This is on the basis that the act of deregistration should not have taken place until after settlement of the property.

The Commissioner has discretion pursuant to s 29-10(3) to allow a recipient of a supply to claim an input tax credit in the absence of a tax invoice. In GSTR 2011/D1 the Commissioner discusses the basis on which this discretion will be exercised.[20] The following paragraphs from GSTR 2000/D1 assist in determining how that discretion may be exercised:

> 94. There may be situations where a document relevant to a taxable supply does not meet all the tax invoice requirements of subsection 29-70(1). In these situations, the requirement to hold a tax invoice may impose a disproportionate burden on a supplier or recipient, particularly if that document substantially complies with the requirements. The Commissioner has the discretion in subsection 29-70(1B) to treat a document or documents as a tax invoice in these situations. However, the Commissioner is under no obligation to exercise the discretion. It is therefore the onus of the supplier or the recipient to demonstrate in their request to the Commissioner that their circumstances make it appropriate for the Commissioner to treat the document or documents as a tax invoice.
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> 95. The relevant principles for making administrative decisions were set out by Mason J in Minister for *Aboriginal Affairs v. Peko-Wallsend Ltd & Ors* (1986) 162 CLR 24, where his Honour said at 39-40:
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> > What factors a decision-maker is bound to consider in making the decision is determined by construction of the statute conferring the discretion... where a statute confers a discretion which in its terms is unconfined, the factors that may be taken into account in the exercise of the discretion are similarly unconfined, except in so far as there may be found in the subject matter, scope and purpose of the statute some

[20] This is only a draft ruling but it replaces GSTR 2000/17 which was withdrawn on 25 May 2011. It is similar to GSTR 2000/17.

> implied limitation on the factors to which the decision-maker may legitimately have regard ...By analogy, where the ground of review is that a relevant consideration has not been taken into account and the discretion is unconfined by the terms of the statute, the court will not find that the decision-maker is bound to take a particular matter into account unless an implication that he is bound to do so is to be found in the subject matter, scope and purpose of the Act.
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> 96. It is therefore important to consider the subject matter, scope and purpose of sections 29-10 and 29-70.[21]

The Ruling states that the issues to be considered before a decision is made to exercise the discretion are contained in Practice Statement LA 2004/11. The practice statement sets out the steps to be taken by ATO staff when deciding to exercise the discretion.

> 26. This situation will usually arise during Tax Office verification activities, but may arise on other occasions, for example when the recipient has discovered the error and brings this to the attention of the Tax Office. In considering the exercise of the discretion, officers must adopt a case by case approach, based on the compliance model. The Tax Office wishes to encourage future compliance as well as uphold the importance of tax invoices and adjustment notes. If there is a creditable acquisition or decreasing adjustment, and the recipient has made a genuine attempt (in their circumstances) to comply, the discretion should be exercised.
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> 27. Officers should ensure that a tax invoice or adjustment note is needed for the recipient to claim the input tax credit or decreasing adjustment. Refer to paragraph 12 for a discussion of when a tax invoice or adjustment note is required.
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> 28. Officers should follow the steps below in deciding whether to exercise the discretion.
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> STEP 1 - Is it reasonable to conclude from the available evidence that the recipient has made a creditable acquisition or has an adjustment from an adjustment event?

the current situation, the purchaser would contend that they made a creditable acquisition in buying the real property for the purpose of conducting an accounting and financial planning practice. At the time of settlement the purchaser was registered for GST and believed that one of the vendors was also registered for GST. The ATO should have answered yes.

> If YES, go to step 2.
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> If NO, the discretion will not be exercised and the recipient must be advised accordingly. Amend the activity statement to disallow the input tax credit or decreasing adjustment.
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> STEP 2 - In the circumstances is it reasonable to exercise the discretion? The key focus here is whether the recipient, through its actions, has made a genuine attempt to meet the requirements to hold a tax invoice or adjustment note. The answer to this question will depend on your judgment. Officers should consider all relevant circumstances, and not irrelevant circumstances when reaching a decision. Some factors which may be relevant are set out in paragraphs 29-30.

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[21] GSTR 2000/D1, paragraphs 94-96.

In the current situation the purchaser made an attempt to obtain a tax invoice from the vendor but was advised that they were no longer registered for GST and could not provide a tax invoice. The purchaser had an excellent record of compliance and this should have been taken into account.

> If YES, exercise the discretion - go to Step 3.
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> If NO, do not exercise the discretion - Go to Step 4.
>
> STEP 3 - If the answer at step 2 was Yes, exercise the discretion to treat a particular document, that was held at the time the relevant activity statement was lodged, as a tax invoice or adjustment note.
> - If there is sufficient evidence to establish a creditable acquisition or decreasing adjustment, there will be some document on which the discretion can operate (for example, invalid tax invoice, normal invoice, contract, etc).
> - The recipient will be taken to have held a tax invoice or adjustment note at the time of giving the GST return in which the credit or decreasing adjustment was claimed. If the other requirements for attribution have been met, the recipient will have made a valid input tax credit claim or decreasing adjustment and there is no need to take any further action in respect of this claim.
> - The recipient must be given clear advice about the requirements to hold a tax invoice or adjustment note and advised to take steps to avoid similar problems in future. If the tax invoice or adjustment note problems are caused by the supplier, and the supplier does not comply in the future, we would expect the recipient to approach the Tax Office in the first instance, before claiming an input tax credit or decreasing adjustment.
> - If the supplier has not issued a valid tax invoice, consider whether to refer details to compliance for possible follow-up action. For example, was the problem a significant one likely to be repeated and cause problems for other recipients?

In the current situation it is contended that the Commissioner should have exercised his discretion and accepted the contract of sale of real property as being equivalent to a tax invoice.

> STEP 4 - If the answer at step 2 was No, do not exercise the discretion. Officers must:
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> - amend the activity statement to disallow the input tax credit or decreasing adjustment.
> - advise the recipient to keep and retain adequate records of their GST transactions and indicate that failure to do so could lead to an administrative penalty.
> - advise the recipient to make a reasonable attempt to obtain a tax invoice or adjustment note from the supplier. What constitutes making a reasonable attempt to request the document is explained at paragraph 25.
> - advise that, if a tax invoice or adjustment note is subsequently obtained, the input tax credit or decreasing adjustment can be claimed in a later activity statement.
> - advise that if the recipient makes a reasonable attempt to request a tax invoice or adjustment note, but is not able to obtain one, they may make a new request for the exercise of the discretion. The recipient's new request should be considered as if the input tax credit or decreasing adjustment had not been claimed before - that is, in accordance with the first flowchart in paragraph 9 and the discussion in paragraph 22-25.
> - consider whether to refer details of the supplier's actions to compliance for possible follow-up action. For example, was the problem a significant one likely to be repeated and cause problems for other recipients?

The ATO did not allow the purchaser to claim an input tax credit and considered imposing a shortfall penalty for making a false or misleading statement.

> In what circumstances would it be reasonable to exercise the discretion for the recipient?
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> 29. If there is a creditable acquisition or decreasing adjustment, and the recipient has made a genuine attempt (in their circumstances) to comply, the discretion should be exercised. The key focus here is whether the recipient, through its actions in the circumstances, has made a genuine attempt to meet the requirements to hold a tax invoice or adjustment note. If not, it may be reasonable to refuse to exercise the discretion. Officers should consider the recipient's circumstances, including the practical and commercial realities of record keeping.

The purchaser contends that they made a genuine attempt to comply with the law and that the actions of the vendors deliberately prevented the purchaser from being able to claim an input tax credit. Therefore in the circumstances, the purchaser contends that the discretion should have been exercised and the input tax credit allowed on the basis that the contract of sale was an adequate substitute.

## III DEREGISTRATION: A LEGITIMATE STRATEGY?

This part of the paper raises the question as to whether it is a legitimate strategy for accountants and lawyers to encourage taxpayers to cancel their GST registration in a situation where a business asset is being sold and GST that should be paid to the ATO is subsequently retained by the vendor. Is this action within the spirit of the law?

The vendor deregistered prior to settlement and as a result did not provide a tax invoice to the purchaser. Quite correctly he was unable to provide a tax invoice. The sale of the property was for the sum of $400,000 and the contract of sale indicated that GST was not included in the price. If GST had been included then the price would have been $440,000. The purchaser contends that the vendor led them to believe that they were registered at the time of entering into the contract and this would be their status up until settlement. If this was the case then why did the vendor not include GST in the price because the premises were commercial premises and as such a taxable supply. The position of the vendor would have been that an extra $40,000 would have been paid by the purchaser; the $40,000 extra collected by the vendor paid to the ATO as GST and the purchaser claiming an input tax credit. However, the vendor cancelled the registration retrospectively which meant that at no time during negotiations for the sale of the real property was the vendor registered for GST. However, in order to obtain deregistration, the vendor gives an assurance that at no time have they held themselves out as being registered for GST. The cancellation process requires the taxpayer signing a declaration that the information is correct. This is a similar declaration that every taxpayer signs when lodging their income tax return or a Business Activity Statement.

Is it therefore a legitimate strategy to have a client deregistered from GST in these circumstances? If the position taken by the ATO is to be accepted, then in this case

the vendor escaped the liability of paying GST to the ATO in the sum of $36,363. Clearly this would prima facie indicate that the action taken by the vendor was completely legitimate. It would also indicate that all accountants and lawyers should advise their clients to cancel their GST registration in similar circumstances. The only issue for the purchaser is that they need to be very clear in their negotiations with a vendor as to the GST status of both parties and if GST is to be included in the price.

## IV CONCLUSION

From the above analysis of the case study it could be inferred that a perfectly legal strategy for a taxpayer to avoid paying GST is to deregister just before settlement of the sale of a business asset. The purchaser will not be provided with a tax invoice and the Commissioner will not exercise his discretion in those circumstances to treat the contract as a tax invoice. However, this case study appears to raise more questions than it does provide answers. Those questions can be summarised as follows:

(i) What role should the ATO take in scrutinising application to cancel GST registration?
(ii) What role should the ATO take in investigating the conduct of the vendors in similar circumstances? Should the activity be referred to the Australian Federal Police for investigation into whether a false or misleading declaration was signed by the vendors?
(iii) Does the conduct of the vendors' amount to false and misleading conduct that should be investigated under the Australian Consumer Law, Schedule 2 to the *Competition and Consumer Act 2010* (Cth)? This would not require involvement by the ATO.
(iv) Should the ATO Practice Statement PS LA 2004/11 be amended to specifically discuss situations where deregistration occurs and the purchaser is not provided with a tax invoice, similar to the circumstances in this case study?

The answers to the above questions are beyond the scope of this paper and require the ATO to consider situations similar to those discussed here. It would appear that the winner is the vendor in that no GST was paid; the winner was also the government's revenue base because the purchaser did not claim an input tax credit; and the looser was the purchaser based on the current application of the GST law to these circumstances. Quite clearly this is one way to legitimately avoid paying GST. There is one important lesson that should gained from reading this paper and that is all purchasers and vendors of real property must openly discuss the issue of GST as it relates to their particular transaction. There must be a clear understanding of the registration status of both parties and whether the price includes GST.