STNS 3 - SALES TAX "USE" IN SALES TAX LEGISLATION

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TAXATION RULING NO. ST NS3

- SALES TAX "USE" IN SALES TAX LEGISLATION

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F.O.I. EMBARGO : May be released

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F.O.I. INDEX DETAIL

REFERENCE NO:	SUBJECT REFS:	LEGISLATIVE REFS:
I 1211602	USE EXCLUSIVELY, PRIMARILY, PRINCIPALLY, MAINLY. GOODS OF A KIND USED, ORDINARILY	SALES TAX (EXEMPTIONS AND CLASSIFICATIONS) ACT; ITEMS 1, 4, 13, 18, 26A, 37, 42A, 54, 61 - 81C, 89, 90C, 107, 108, 113, 114B, 119, 119C, 139, 158, FIRST SCHEDULE; ITEM 44, SECOND SCHEDULE; ITEM 1, THIRD SCHEDULE.

PREAMBLE UNDERSTANDING THE TERM "USE" IN THE SALES TAX LEGISLATION

Why is use important?

1.1 The amount of sales tax payable on goods frequently depends in some way on the use of the goods. Many of the sales tax provisions contain the word "use" or some variation of it, either as a condition of exemption or in other ways. Therefore, knowing how to interpret the provisions dealing with use will help you determine whether the goods are exempt from sales tax, or whether tax is payable at a particular rate.

What does the Ruling do?

1.2 "Use" is a very general word. It cannot be precisely defined, nor can another word or phrase always be substituted for it (1). Often the word will take its meaning from the context in which it appears or the qualifying words which appear with it. This Ruling sets out the Taxation Office view of the principles which apply when interpreting a sales tax provision which refers to use. It is a guide rather than a reference work for specialists in sales tax interpretation and is therefore expressed in non-technical language where possible.

1.3 Various paragraphs of the Ruling contain examples to illustrate the principle stated. The examples most often refer to exemption items, meaning, items in the First Schedule to the Sales Tax (Exemptions & Classifications) Act 1935 ("the Classifications Act"). However, the comments also apply to references to use in the other Schedules and elsewhere in the Sales Tax Legislation. The examples are current as at the date of issue of the Ruling, but you should treat them as indications of the general principles only, as they may be affected by subsequent legislative changes.

1.4 The Ruling replaces any previous advice that you may have been given only if that advice is inconsistent with the Ruling. If you are acting on advice that is consistent with principles in the Ruling you need not seek confirmation of that advice. Paragraph 4.1 gives more detail about the previous advice affected.

How do you use the Ruling?

1.5 The Ruling comprises two main sections. Chapter 2 introduces the category of conditional exemption and gives some examples. Conditional exemption is a familiar concept for both taxation officers and practitioners in the sales tax field, although the term is not used in the legislation. The distinction between conditional exemption items and other exemption provisions provides a useful framework for understanding the term use.

1.6 Chapter 3 sets out the principles for determining the meaning of the words and phrases in the exemption provisions. It addresses such practical issues as the degree of a particular use required for goods to be

exempt and the effect of concurrent and consecutive uses.

1.7 Ruling ST (NS) 4 sets out the practical steps you should take in approaching the question of classifying (i.e. determining the rate of tax on) goods. When read in conjunction, these two Rulings provide a comprehensive guide to the Taxation Office view of how to determine the rate of sales tax payable on particular goods.

1.8 For anyone wishing to refer to the authority behind the principles stated in this Ruling, court decisions, other authorities and comments relating to the principles are referred to in footnotes.

HOW THE "USE" OF GOODS AFFECTS EXEMPTION

Exemption Categories

2.1 The exemption items in the First Schedule to the Classifications Act may be divided into two broad categories (2). For convenience, these may be described as:

- conditional items; and
- others.

2.2 Sometimes the second category is labelled as unconditional. This term is not used in this Ruling as even with these items, exemption will depend on certain criteria, so they are conditional in one sense.

Conditional Exemption Items

2.3 In this Ruling, the term conditional refers to an item where the exemption is conditional upon the intended or proposed use of the goods. The two most common types of conditional items are:

- those where exemption depends on the use to which the goods are to be put (for example, goods for use in the production of motion picture films, item 107, or channelling for use for irrigation, subitem 18(1A)); and

- those requiring that a particular person or organization uses the goods (for example, goods for use by the Reserve Bank of Australia, item 76).

2.4 Sometimes use is the basis for exemption, as in the examples above. At other times it is a basis for exclusion from an exemption, as in item 119: ships, not including those to be used for pleasure or sport.

2.5 Perhaps the most frequently occurring wording of conditional items refers to goods for use in an activity. Where an item refers to use in an activity, or use in connection with an activity, entitlement to exemption depends on identifying both the activity referred to and the connection between that activity and the use of the goods (3). Both are matters of fact and degree, which will differ from case to case. The approach is illustrated by the example in the following paragraph.

2.6 Item 1 of the First Schedule exempts a list of particular goods under the category:

> "Agricultural machinery, implements and apparatus... for use in agricultural industry..."

For listed agricultural machinery to be exempt, the activity must first meet the description of agricultural industry. Thus, for example, a person who gardens as a hobby is not entitled to exemption because the activity does not satisfy the description of agricultural industry. Secondly, the machinery must be used in the activity. Usually this will mean that the machinery must be used in the course of carrying out that activity. Accordingly, a farmer (who is engaged in agricultural industry) cannot get exemption for goods listed in item 1 if he is to use them solely for private purposes as they would not be used in the course of his farming activity.

2.7 Often the expressions for use in and used in activities such as agriculture or manufacture will mean that the goods in question facilitate the activity without being consumed in the process. The expression used in is also found in the phrase "used in, wrought into or attached to" other goods (as for example, in item 113, materials... used in, wrought into, or attached to, so as to form part of, goods to be manufactured...). Here the expression means incorporated into the goods specified (4). In other cases, the context will indicate whether the exemption item refers to goods which are consumed or goods which facilitate a process (5).

2.8 A few items in the First Schedule exempt goods which are for use for a special purpose, are used to do something, or are for use as a particular thing. Unless otherwise qualified, exemption under these items will depend upon the same factors as for the phrase for use in. However, occasionally there will be other qualifiers indicating that the intended use of the goods by the end user will not determine exemption. For example, item 26A exempts certain oils put up for use for culinary purposes. The effect of the words "put up for" is that the oil must be sold as suitable for that purpose. Thus, a motor oil could not qualify for exemption under this item, even in the unlikely event that someone intended to use it to cook with.

2.9 Exemption items depending upon use by a person or organization are also common. These are principally found in items 61 - 81C and the miscellaneous items at the end of the First Schedule. To determine exemption under these items it is necessary to -

- identify the characteristics of the specified user, for example, what comprises a school (item 63A) or a State public library (item 74A)?;

- determine whether the particular user meets that description; and

- establish that the goods will be used by the exempt user.

These are all questions of fact and degree (6). More information about exemptions available for particular organizations is contained in Rulings ST (NS) 3002, 3003 and 3004 (dealing with Public Benevolent Institutions, schools and churches respectively).

2.10 Some conditional exemption items contain the term official use (for example, articles... for the official use of... the Governor-General, item 73A and, goods for official use... by a department of the Government..., item 74). In this context, the word official is used simply to distinguish exempt goods from goods which are for the personal use of the individual referred to, or for unauthorised use by individuals within the organization.

Other Exemption Items

2.11 In other items, exemption is not conditional upon the use to which the actual goods in question will be put, but depends upon an attribute or common feature the goods have. Exemption can apply in these other items according to:

- the character or description of the goods (for example, newspapers, item 54, or tobacco, item 37(1));
- whether the goods are of a kind which is used in a particular way (for example, materials of a kind used... as ingredients of concrete, subitem 89(4)); or
- whether goods are marketed in a particular way (for example, goods marketed exclusively or principally as food for birds, item 108).

2.12 Items conferring exemption on goods of a particular character will not usually contain the word "use", however, even in these items the intended use of goods may be relevant. For example, the intended use of a weekly publication was taken into account in concluding it was not a "newspaper" (7) and therefore not exempt.

2.13 Apart from the items which allow exemption according to the character of goods, it is common for items to refer to goods of a kind used. This phrase means that it is not the intended use of the actual goods to be classified which is important, but whether they fall into a particular class of goods.

2.14 The items using the phrase of a kind may refer to goods generally, or specify particular types of goods, e.g. road vehicles of a kind. In either case, you should look at the qualifications specified in the item (e.g., subitem 90C(1), "electrical fittings... being goods of a kind used... as part of fixed electrical installations in consumers' premises... ") to see what common

characteristics identify the goods comprising the specified kind. Having identified the kind of goods exempted, the question is then whether the particular goods to be classified are of that kind. Both the question of the nature and limits of the "kind" of goods specified by the item, and the question whether the particular goods under consideration fall within that "kind", are matters of fact and degree (8).

2.15 Often the word ordinarily (9) will appear in conjunction with the phrase "goods of a kind" (for example, goods... of a kind ordinarily used for household purposes..., item 1, Third Schedule). Goods are of a kind ordinarily used in a manner or for a purpose if that is a manner or purpose commonly, routinely or usually encountered for that class of goods.

2.16 When an item sets out a marketing test such as the one in item 108 (goods marketed... as food for birds), it does not confer exemption according to the actual use to which the goods will be put. The test is met when the goods are marketed in the required way, irrespective of their actual use.

Overlap between Categories

2.17 In many items, the various tests described in paragraphs 2.3 to 2.16 overlap. For instance, exemption can depend on meeting both a test as to the character of the goods and a condition regarding their use. Examples of overlapping tests include item 119C, omnibuses for use in transporting passengers for reward, and subitem 13(1), machinery... for use in agricultural industry if... they are goods of a kind used... in that industry).

PRINCIPLES FOR DETERMINING EXEMPTION ACCORDING TO USE

What does "use" mean?

3.1 As mentioned in paragraph 1.2, the word "use" is so general and is used in so many contexts that it cannot be precisely defined in a single way to fit them all. In the Sales Tax Legislation it sometimes appears as a verb (used or to be used) and at other times as a noun (in use, for use). When used as a verb, the meaning is generally "to employ for a purpose or in a fashion". When used as a noun, the sense is that of utilisation, employment or application. The questions of when use is ascertained, how much use is required to qualify and the effect of other uses are dealt with in the following paragraphs.

When do you determine the use?

3.2 Liability for sales tax ordinarily arises when the last wholesale sale occurs, a time which may be well before the use spoken of by an exempting item (10). Therefore, exemption must be determined according to what the purchaser intends to do with the goods in the future (11). For example, when a farmer claims exemption on ordering a new tractor (subitem 1(48)), he is assuring the vendor

(and the Taxation Office) that he intends to use it in his farming activities in the future and exemption applies on the basis of that assurance.

3.3 In most cases the intended use of the goods will reflect what actually happens to them. However, it is possible that the intention may never be given effect without exemption being lost. Thus, equipment may be exempt as for use by a hospital (item 81) although it goes into storage immediately after purchase and eventually becomes obsolete before it is able to be used. The fact that the equipment was not actually used by the hospital in this example would not affect the entitlement to exemption, as it was purchased with the bona fide intention that it would be so used.

3.4 Although, as with the example in the previous paragraph, exemption may apply despite the fact that an intention may never be given effect to, it is important to remember that the intention should be capable of objective verification later in order to establish that it is bona fide. When an exemption claimed is reviewed after the fact in a sales tax audit, how or by whom the goods were used can be taken into account as some indication of what was the intended use of the goods at the time of the taxable dealing. If the use to which the goods were actually put was not a use which would qualify the goods for exemption, the person who has claimed exemption may be asked to explain why it applies.

3.5 Usually when exemption depends on the use to which the goods will be put, or the identity of the user, that use will be clearly apparent at the time the liability arises (12). However, sometimes the issue of exemption must be examined with hindsight. An example of this would be when a retailer buys stationery, paying tax on the purchase, but later sells it to a school for its use. The sales tax regulations allow for refunds in some circumstances where a sales tax liability has arisen, but the goods are later dealt with in exempt circumstances. An explanation of the circumstances in which refunds apply will be the subject of a future sales tax Ruling.

How much use to qualify?

3.6 Usually, the degree of use can be measured solely in terms of the time that the goods are to be used. However, whilst the amount of time the goods are to be used is probably the most common form of measurement, the legislation does not specify any particular way. What is important is that the person claiming exemption intends that the use will be sufficient to qualify and has a reasonable basis for forming that intention. Thus, a harvester will be exempt under subitem 1(37) as for use in the agricultural industry because it plays a vital role in the farming operation, even if most of the time during the year it remains idle.

3.7 A number of items specify a rule as to the amount of use required for exemption. This is done by the inclusion of words or phrases to qualify the degree of use. Words

such as "mainly" and "exclusively" and phrases such as "primarily and principally" qualify the degree of use required in order for the goods to be exempt (13). The effect of these words and phrases is outlined in paragraphs 3.8 to 3.11.

3.8 "Mainly":

"Main" is defined in the interpretation clause of the First Schedule to the Classifications Act as meaning not less than 50%. A requirement that goods be used mainly in a certain way, generally means that at least half of the time they are used, they are used in that particular way. Theoretically it is possible for goods to have two main uses, each having a 50% use.

Mainly is a recently introduced term and therefore occurs infrequently. An example of where it appears is item 158 (goods... for use by a person... mainly in carrying out activities... on behalf of... manufacturers).

3.9 "Exclusively" (14):

When this word is used to qualify the use of the goods, it means that the goods should not be for use in any other way or for any other purpose.

Exclusively appears on its own as a qualifier rarely. An example is subitem 139(1) (preparations and materials for use exclusively in the destruction of insect pests... for business... purposes).

3.10 "Primarily and Principally" (15):

For goods to be used primarily and principally for a particular purpose or in a particular way, that use must be the most important or most significant of all the intended uses. A primary and principal use must exceed any other and, whilst it need not account for a majority of the use of the goods, it will usually do so. Primarily and principally have such similar meanings, that the presence of the two of them in conjunction adds nothing to the meaning of principally by itself.

3.11 The three words exclusively, primarily and principally occur in various combinations, for example:

- exclusively, or primarily and principally (subitem 4(2));
- exclusively or principally (item 42A);
- primarily or principally (item 44 of the Second Schedule); and
- principally (item 18(1)).

In practice, all these expressions have the same meaning. Each qualification will be met when the goods are primarily and principally used (as defined in paragraph 3.10) in the specified way.

3.12 When an item refers to "use" without further qualification (e.g. agricultural machinery... for use in

agricultural industry, item 1), the use must be an appreciable or significant use of the goods, not merely a possible or remote use of them (16). Significance is determined having regard to the nature of the goods, their expected service life and the extent, nature and duration of the qualifying use.

3.13 It should be remembered that during a sales tax audit it may be necessary to explain how the exempt use is sufficient to meet the test of significance or other qualification set out in the words of the item.

Concurrent Use

3.14 Whilst some goods are only ever to be put to a single use by a single person during their effective lifetime, other goods may be for use in more than one way or by more than one person at a time. This can arise when there is to be an active use of the goods as well as a passive one (17). For example, elevators in a multi-storey office building can be said to be used passively by the owner of the building as well as actively by the tenants of the various floors.

3.15 Goods which qualify for exemption by reason that they are to be used by a particular user do not lose exemption simply because they are to be used by others in non-exempt circumstances as well. The question is simply whether the exempting use is sufficient to meet the test set out in the item under consideration having regard to the nature of the goods, their expected service life and the extent, nature and duration of the qualifying use. Thus, for example, elevators in a multi-storey building owned by a State Authority (item 74) would not lose exemption simply because a tenant on one of the floors of the building was not an exempt organization.

3.16 Although it is less common, goods which are owned by a non-exempt user may become exempt by reason that they are made available for use by an exempt user. An example of this would be rubbish bins owned by a contractor, but committed to use by a local council (item 78) under the terms of a contract between the two parties.

Consecutive Uses

3.17 It often happens that, within a fairly short time of going into consumption, goods are used by more than one person or in more than one fashion. This may happen either by choice or because of an unforeseen change in circumstances. If goods are exempt when acquired, a subsequent change to a non-exempt use due to unforeseen circumstances will be irrelevant. However, if the subsequent use was one foreseen at the taxing point, the goods will only be exempt if the qualifying use was intended to be sufficient to meet the test of the item.

3.18 If, for example, a United States serviceman purchased a motor vehicle intending to use it himself then sell it later, the vehicle might be exempt under item 114B depending on whether the exempt use is significant (as

the test in this item is simply use without other qualifications). If the serviceman was to use the vehicle for the three years remaining in his tour of duty, that would no doubt be a significant use and the test set out by the item would be met. If however, he intended only to use it for three days, or for a single journey of 500km and then sell it, that use could not be regarded as significant in terms of the life of the car and exemption would not apply.

3.19 Between these extremes, there are many possibilities. Exemption will depend on the facts in each circumstance, but as a general rule, it should not be assumed that exemption will apply when it is known that goods will be put to a non-exempt use either shortly after purchase or while the goods still have the majority of their useful life ahead.

Special note on Motor Vehicles:

3.20 Motor vehicles are a source of common enquiry as they are almost always purchased with the expectation that they will later be sold while still having a long service life. As a guideline for people purchasing a vehicle in exempt circumstances, the Taxation Office accepts that where a motor vehicle is in fact used in exempt circumstances for the first two years after purchase or to travel the first 40,000km, that use will be regarded as significant. Of course, lesser uses may qualify depending on the circumstances. This guideline simply provides an assurance that the significance of the use will be accepted in the event of an audit.

DOCUMENTS, DECISIONS AFFECTED BY THIS RULING

4.1 This Ruling will affect previously issued documents and decisions in the following manner:

(a) The document in the Freedom of Information Index listed at Appendix A is superseded.

(b) The paragraphs of Australian Sales Tax (A.G.P.S. Canberra, 1984) listed at Appendix A no longer apply. Comments in other paragraphs which may be inconsistent with this Ruling are amended to the extent of the inconsistency.

(c) All private rulings previously issued are amended to the extent they are inconsistent with this Ruling.

COMMISSIONER OF TAXATION
11 July 1991