# *GSTR 2001/D2 - Goods and Services Tax: when is a 'supply of a going concern' GST-free?*

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There is an Erratum notice for this document.
This document has been finalised.

# Draft Goods and Services Tax Ruling
Goods and Services Tax: when is a 'supply of a going concern' GST-free?


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***Preamble***

*This document is a draft for industry and professional comment. As such, it represents the preliminary, though considered, views of the Australian Taxation Office. This draft may not be relied on by taxation officers, taxpayers and practitioners. When officially released it will be a public ruling for the purposes of section 37 of the* ***Taxation Administration Act 1953*** *and may be relied upon by any person to whom it applies.*

## What this Ruling is about

1. This Ruling explains what is a 'supply of a going concern' for the purposes of Subdivision 38-J of *A New Tax System (Goods and Services Tax) Act 1999* ('GST Act'). It also explains when the 'supply of a going concern' is GST-free for the purposes of the Subdivision.

2. The Ruling is intended to provide guidance on the application of the going concern provisions. It does not discuss the application of the provisions to specific industries. However, the examples used in the Ruling do illustrate the application of relevant principles to particular factual circumstances relating to some industries.

3. The Ruling confirms that the going concern provisions are to be considered from the perspective of the supplier.

4. This Ruling does not discuss the supply of farm land under Subdivision 38-O of the GST Act.

5. Although Divisions 129 and 135 are mentioned in the Background section of this Ruling, the Ruling does not discuss adjustments under these provisions.

6. All legislative references in this Ruling are to the GST Act, unless otherwise stated.

# Date of effect

7. This Ruling, when finalised, will apply on and from 1 July 2000.

# Background

8. Subdivision 38-J of the GST Act provides that, if certain conditions are satisfied, a 'supply of a going concern' is GST-free. This means that, in the case of a supply which would otherwise be a taxable supply, or an input taxed supply, the supply is GST-free if it is supplied under an arrangement for the 'supply of a going concern'.

9. The term 'supply of a going concern' is a statutory term which is defined for the purposes of Subdivision 38-J of the GST Act in subsection 38-325(2):

> (2) A ***supply of a going concern*** is a supply under an arrangement under which:
>
> (a) the supplier supplies to the *recipient all of the things that are necessary for the continued operation of an *enterprise; and
>
> (b) the supplier carries on, or will carry on, the enterprise until the day of the supply (whether or not as part of a larger enterprise carried on by the supplier).[1]

10. The ordinary meaning of the term 'going concern', which is often used in reference to the activity of a business, does not necessarily correspond to the statutory definition. The elements of the statutory definition are discussed in detail in this Ruling.

11. The application of Subdivision 38-J means that the recipient does not have to obtain additional funds to cover the GST that would otherwise be included in the price of a going concern if the Subdivision did not apply.[2]

12. Subsection 38-325(1) provides:

> (1) The supply of a going concern is ***GST-free*** if:
>
> (a) the supply is for consideration; and
>
> (b) the recipient is registered or required to be registered; and

[1] Asterisks refer to definitions in section 195-1 of the GST Act
[2] Explanatory Memorandum to the A New Tax System (Goods and Services Tax) Bill 1998.

(c) the supplier and the recipient have agreed in writing that the supply is of a going concern.

13. A recipient of a 'supply of a going concern' that intends to make supplies which are neither taxable nor GST-free may be required by section 135-5 to make an initial increasing adjustment.

14. The recipient of a 'supply of a going concern' is required to make a further increasing or decreasing adjustment under section 135-10 where the proportion of the supplies made through the enterprise which are neither taxable nor GST-free has changed from the proportion of intended supplies. Section 135-10 requires that, in these circumstances, an increasing or decreasing adjustment is to be made using the method contained in Division 129.

# Ruling and Explanations

**What is a 'supply of a going concern'?**

15. The statutory term 'supply of a going concern' is defined in subsection 38-325(2) as a supply under an arrangement under which:

(a) the supplier supplies to the recipient all of the things that are necessary for the continued operation of an enterprise; and

(b) the supplier carries on, or will carry on, the enterprise until the day of the supply (whether or not as a part of a larger enterprise carried on by the supplier).

16. There may be several supplies, each of which is a 'supply of a going concern' under the one arrangement. For the purposes of the definition of a 'supply of a going concern', it is not a supply itself which must satisfy the conditions in paragraphs 38-325(2)(a) and (b), but the arrangement under which a supply is made. A supply is the 'supply of a going concern' where:

(i) there is an arrangement which satisfies paragraphs 38-325(2)(a) and (b), and

(ii) the relevant supply is made under that arrangement.

17. An arrangement satisfies paragraph 38-325(2)(a) where each of the following elements is present:

- the supplier supplies to the recipient;
- all of the things that are necessary for the continued operation;
- of an enterprise.

18. Paragraph 38-325(2)(b) of the definition also requires two additional elements to be present:

- the supplier carries on, or will carry on, the enterprise;
- until the day of the supply.

**What is a 'supply under an arrangement'?**

19. A supply is defined in section 9-10.

20. The term 'supply under an arrangement' includes a supply under a single contract or supplies under multiple contracts which comprise a single arrangement. However, the things supplied under the arrangement must relate to the same enterprise, that is, the enterprise referred to in paragraphs 38-325(2)(a) and (b) (the 'identified enterprise').

21. The supplier and the recipient may identify the arrangement and the supplies under the arrangement, in the written agreement which is required under paragraph 38-325(1)(c) or in any other written agreement that relates to the arrangement. However, an arrangement between a supplier and a recipient is characterised not merely by the description which both parties give to the arrangement, but by looking at all of the transactions entered into and the circumstances in which the transactions are made.

**What is the 'enterprise' referred to in paragraphs 38-325(2)(a) and (b)?**

22. Paragraphs 38-325(2)(a) and (b) require the conditions to be satisfied in relation to an 'identified enterprise'.

23. The term 'enterprise' is defined in section 9-20 as an activity, or series of activities, done:

- in the form of a business; or
- in the form of an adventure or concern in the nature of trade; or
- on a regular or continuous basis, in the form of a lease, licence, or other grant of an interest in property; or
- 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 *Income Tax Assessment Act 1997* and to which deductible gifts can be made; or
- 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

- by a charitable institution or by a trustee of a charitable fund; or
- by a religious institution; or
- 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.[3]

24. The meaning of the term 'enterprise' is wider that the meaning of the term 'business'. For example, the activity of leasing can be the subject of the 'supply of a going concern'.

*Example: Fully tenanted building*

25. Digger Co. owns a small retail shopping complex that has been fully tenanted for many years. For the purposes of the definition of 'enterprise' in section 9-20, Digger Co. is carrying on an enterprise of leasing the complex because it carries on leasing activities on a regular or continuous basis.

26. Subsection 38-325(2) requires the identification of an enterprise that is being carried on by the supplier (the 'identified enterprise'). This is the enterprise for which the supplier must supply all of the things that are necessary for continued operation. Also, the supplier must carry on this enterprise until the day of the supply, whether or not as part of a larger enterprise.

27. Where the enterprise identified for the purpose of subsection 38-325(2) forms part of a larger enterprise, a supply is a 'supply of a going concern' when all of the things necessary to continue the operation of that part of the enterprise as an independent enterprise are supplied.

*Example: An enterprise within a larger enterprise*

28. Stay-Puff Bakeries is a chain of retail bakeries conducted by Pufferies Pty Ltd ('Pufferies'). Pufferies sells the bakery operating in a particular suburb to Pies and Things partnership. All of the things necessary for the continued operation of the bakery are supplied under the arrangement. As the bakery is part of the enterprise being conducted by Pufferies and is capable of operating as an independent enterprise, each of the supplies made under an arrangement to supply all of the things that are necessary for the bakery business may be the 'supply of a going concern'.

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[3] Refer to Goods and Services Tax Determination GSTD 2000/8 and Taxation Ruling MT 2000/1.

29. Where the thing supplied is merely an asset used in an activity that is carried on as an enterprise, the supply of that asset is not the 'supply of a going concern'.

*Example: Supply of an asset which is not an enterprise in its own right*

30. Insurance Co. is an entity which owns the building from which it operates its insurance business. Insurance Co. enters into a contract to sell the building to Landlord Unit Trust and agrees to enter into an agreement to lease the building back from the trust. Whilst Insurance Co. carries on an enterprise of conducting an insurance business from the premises, Insurance Co. does not at any time conduct an enterprise of leasing the premises.

31. Insurance Co. did not (and could not) conduct an enterprise of leasing to itself prior to the day of the supply and merely supplied Landlord Unit Trust with an asset used by Insurance Co. in the conduct of its enterprise. Although the recipient commenced to carry on an enterprise of leasing after the day of the supply, the supply of the premises cannot be the 'supply of a going concern' because no enterprise of leasing had been operated by the supplier. That is, Insurance Co. could not satisfy the requirement that an enterprise be carried on to the day of the supply (paragraph 38-325(2)(b)) because there was no enterprise of leasing carried on by the supplier, Insurance Co. Further, the supplier cannot supply all of the things that are necessary for the *continued operation* of an enterprise that was not carried on prior to the day of the supply (paragraph 38-325(2)(a)).

32. A supply of a thing necessary for the continued operation of an activity which is part of an enterprise cannot be the 'supply of a going concern' unless the conduct of the activity is itself an 'enterprise' as defined in section 9-20 of the GST Act.

*Example: Supply of an activity which is not an enterprise in its own right*

33. ABC NL ('ABC') is a large public company engaged in the mining industry. A decision is made to outsource its information technology ('IT') services to a private company, ServiCo. Prior to outsourcing taking place, the IT function within ABC is performed by its own employees. ABC does not maintain a separate accounting system nor is there any internal user charging for the provision of the IT function. The employment of staff performing the IT function is terminated and some staff are offered employment by ServiCo. ServiCo leases office accommodation within the ABC building and purchases all of the relevant equipment and software from ABC.

34. The IT services function of ABC was not capable of being an enterprise in its own right because it was not operated in the form of a business or in the form of an adventure or concern in the nature of trade. This is not the 'supply of a going concern'.

35. On one view, no enterprise is being carried on where the internal division does not make supplies to external clients. Such a construction would mean that many sales of distinct parts of a larger enterprise, including privatisations of public infrastructure, would not get the benefit of Subdivision 38-J. However, use of the term 'in the form of' in paragraph 9-20(1)(a) suggests that not all of the features of a business need to be present.

*Example: Part of an enterprise which is an enterprise in its own right*

36. Zinco is a manufacturer of metal products which uses a large amount of electricity for its processes. Zinco has its own power generation plants to ensure that it has sufficient electricity supplies at all times. The power generation activity is a separate division with substantial operations which are separate and distinct. The power generation division has a separate management structure and a considerable degree of autonomy within the company structure. It does not deal with nor generate any revenue from external customers but supplies the power it generates to other divisions under internal service agreements. It has a system of internal user charging for those services.

37. Zinco sells the power generation activity to an independent power provider. Zinco transfers the plant and premises which are used in power production, the benefit of existing contracts with external suppliers, separate management structure and facilitates the transfer of relevant employees. As a part of the sale agreement, a contract is entered into under which the power provider is to supply electricity to Zinco.

38. Because Zinco is conducting the power generation operations as a separate division and in the form of a business within its larger enterprise, the activities of that division may be an enterprise. The supply of the power generation operation is the 'supply of a going concern' provided the activity of power generation is conducted by Zinco up to the day of the supply and all of the things that are necessary for the continued operation of the division are supplied to the recipient.

### What is meant by 'the supplier supplies'?

39. This term emphasises that the elements of paragraph 38-325(2)(a) must be satisfied from the perspective of the supplier.

The ability of the recipient to provide some of the things necessary for the continued operation of the enterprise is not a relevant consideration.[4] The requirements in paragraphs 38-325(2)(a) and (b) must be met by the same single supplier. Section 23 of the *Acts Interpretation Act 1901* provides rules as to gender and number. It states:

> 23 In any Act, unless the contrary intention appears:
>
> (a) words importing a gender include every other gender; and
>
> (b) words in the singular number include the plural and words in the plural number include the singular.

40. In our view, a contrary intention is evidenced by the words used in Subdivision 38-J. Subsection 38-325(2) requires an entity to conduct the enterprise which is to be carried on until the day of the supply. It follows that the supplier is *an* entity (singular) as only *an* entity can carry on *an* enterprise[5].

41. Similarly, the requirement in paragraph 38-325(2)(a) can only be met where a single entity is the recipient of the supply. This is because the supplier must supply all of the things that are necessary for the continued operation of the 'identified enterprise' to the recipient and the recipient must be put in a position on the day of the supply where it can, if it so chooses, continue to operate that enterprise. Only *an* entity can operate *an* enterprise and the supplier cannot put more than one recipient in a position to operate a single enterprise.

42. A GST group is treated under Division 48 as a single entity for specific purposes.[6] The purposes for which a GST group may be treated as a single entity do not include the supply or receipt of supplies under an arrangement for the 'supply of a going concern'.

43. In some circumstances, it may not be possible for a supplier to transfer or convey some of the things necessary for the continued operation of an enterprise. For example, in some States, a logging licence cannot be assigned and must be surrendered before a new licence is issued by the relevant authority.[7] Similarly, the benefit of certain contracts are not assignable because of the nature of the contract itself, for example, employment contracts, or because of

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[4] *Belton v. CIR* (1997) 18 NZTC 13 403; *Allen Yacht Charters Ltd v. CIR* (1994) 16 NZTC 11 270.

[5] A partnership or other entity as defined in section 184-1.

[6] For example, in relation to supplies and acquisitions made wholly within a GST group.

[7] See, for example, the discussion in *Marbut Gunnersen Industries Pty Ltd v. FC of T* 82 ATC 4182; (1982) 12 ATR 926.

limitations which are imposed under the relevant contract, e.g., franchise agreements.

44. Because the relevant thing which is incapable of assignment is necessary for the continued operation of an enterprise, it is arguable that the supplier is unable to supply one of the necessary things. A narrow or technical construction of the term 'supplier supplies' leads to a conclusion in these circumstances that the supplier would not have supplied a thing which is necessary where the thing has in fact been supplied to the recipient by a third party.

45. The better view, however, is that the surrender of the relevant licence, permit or quota is, in substance, the supply of that thing which is necessary for the continued operation of the enterprise in circumstances where it is highly probable that the licence, permit or quota will be automatically reissued by the relevant government or agency. Where the relevant thing is the rights under an existing contract, the surrender of those rights, in circumstances where the third party has committed to enter into a contract under which substantially similar rights will be created in favour of the recipient, will satisfy the requirement that the relevant thing is supplied.

46. The requirement that the supplier supply the relevant thing will not however be satisfied where the supplier simply chooses not to supply that thing. Further, the relevant thing is not supplied if the statutory authority or the third party does not supply that thing to the recipient.

47. The supply of a thing which is necessary for the continued operation of an enterprise by a party other than the supplier is a substantive supply to the recipient of that thing in the following limited circumstances:

- the thing must be incapable of assignment because of a statutory or legal impediment;
- the supplier must make all reasonable efforts to have the thing supplied to the recipient;
- the supply must be by the statutory authority or other party to the contract with the supplier;
- normal commercial practice dictates that the supply can only be effected in this way[8]; and
- the thing must actually **be** supplied to the recipient.

[8] *Marbut Gunnersen Industries Pty Ltd v. FC of T* 82 ATC 4182; (1982) 12 ATR 926.

*Example: Surrender of licence is sufficient*

48. Totenwood Pty Ltd ('Totenwood') conducts an enterprise of sapling removal from pastoral properties. It is required to have a licence from the relevant State authority to remove native trees. The licence is not able to be transferred to another entity without the permission of the State authority. In practice, approval by the State authority is not given. However, when a licence is surrendered, it is reissued to the potential transferee in all but exceptional cases.

49. Totenwood enters into an agreement with Tree-Away Pty Ltd ('Tree-Away') for the sale of the enterprise as a going concern. All of the things that are necessary for the continued operation of the enterprise (e.g., machinery, advertising material, client lists), other than the licence, are supplied under the agreement.

50. Totenwood applies to the relevant State authority for permission to transfer the licence and is refused in accordance with usual practice. Totenwood effects the supply of the licence to Tree-Away by surrendering the licence and asking the State authority to reissue it to Tree-Away.

51. As there was a statutory impediment to the transfer of the licence, and Totenwood made all reasonable efforts to have the licence transferred, the surrender of the licence and its reissue to Tree-Away was the supply of the licence by the supplier.

*Example: Surrender of lease is not sufficient*

52. Cleaver and Son is a partnership which operates an enterprise of retail meat sales from premises leased from Monitor Trust. The terms of the lease agreement permit the assignment of the lease with the approval of the landlord which may not unreasonably be withheld.

53. Cleaver and Son enter into an agreement to sell the enterprise to Fillet Pty Ltd ('Fillet'). The agreement is for the supply of the things that are necessary for the continued operation of the enterprise, including plant and equipment, stock, trade name and advertising, but excluding the assignment of the lease. The partners decide that the partnership will terminate the lease on the day of settlement of the sale, and get a written undertaking from the landlord that it will enter into a new lease with Fillet.

54. As there was no legal impediment to the supply of the lease by Cleaver and Son to Fillet, and the partnership chose not to assign it, the surrender of the lease by the supplier and the agreement by the lessor to enter into a new lease will not be the supply of the lease by the supplier.

**All of the things that are necessary for the continued operation of an enterprise**

55. The term 'necessary' incorporates every attribute of an enterprise that is essential for the continued operation of the 'identified enterprise'. This will depend on the nature of the enterprise carried on and the core attributes of that enterprise. The term 'all of the things that are necessary' does not refer to every conceivable thing which might be used in the 'identified enterprise'. Access to environmental factors, for example, access to public roads, public telephone systems and postal services, are not ordinarily things which must be supplied by the supplier.

56. A 'thing' is necessary for the continued operation of an 'identified enterprise' if the enterprise could not be operated by the recipient in the absence of the thing. For example, a boat may be essential to the conduct of the businesses of a professional fisherman, a water-ski instructor, a deep-sea diving instructor or a repairer of underwater structures because, in most instances, the relevant business could not be conducted at all without a boat.[9]

57. The supplier is required to supply to the recipient all of the things that are necessary to carry on the 'identified enterprise' so that the recipient is in a position to carry on the same enterprise if it chooses.

58. Two elements are essential to the operation of an enterprise:

- the assets necessary for the continued operation of the enterprise including, where appropriate, premises, plant and equipment, stock-in-trade and intangible assets such as goodwill, contracts, licences and quotas; and
- the operating structure and process of the enterprise consisting of the commercial or economic activity relevant to the type of enterprise being conducted, for example, ongoing advertising and promotion.[10]

59. In the New Zealand case *Allen Yacht Charters Ltd v. CIR* (1994) 16 NZTC 11 270, the Court was asked to consider whether the sale of a yacht charter business was a supply of a taxable activity as a going concern for the purposes of the former subsection 11(1) of the New Zealand *Goods and Services Tax Act 1985.*

60. In holding that the sale of a yacht and equipment by the vendor of a yacht charter business, without a transfer of goodwill or of forward bookings, was not the supply of a taxable activity as a going concern, the Court observed:

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[9] *Case R63* 84 ATC 457.
[10] *Case M89* (1990) 12 NZTC 2556.

> 'In this case the "going concern" consisted of two elements. One was the assets necessary for the business or undertaking, namely Chateau Briand and the equipment on her, together with the Ministry of Transport survey and the berth on Z pier. The other is what Barber DCJ described in *Case M89* (1990) 12 NZTC 2,556 at p 2,561 … as the business structure and process that had been operated by the objector with the emphasis on the process rather than the structure.'

61. The supplier supplies all of the things that are necessary for the continued operation of an enterprise when the supplier supplies those things which will put the recipient into a position to continue the enterprise, if it chooses.

62. The intended and actual use by the recipient of all of the things supplied are not relevant in determining if a particular supply is a 'supply of a going concern'. The enterprise may be continued as a different enterprise, as part of a larger enterprise, or may not be continued at all by the recipient.[11]

63. The term 'thing' is defined in section 195-1 as anything that can be supplied or imported. The things which are necessary for the continued operation of an 'identified enterprise' will vary according to the nature of the enterprise and the thing supplied.

64. A number of things which are commonly necessary are discussed in the following paragraphs (refer paragraphs 72-114), but not all of these things will always be necessary for the continued operation of a particular enterprise.

65. Certain things which are used in the enterprise as a matter of choice by the entity conducting the enterprise are not necessary in circumstances where the enterprise can be carried on in the absence of those things, that is, they are not essential.

*Example: Things that are not necessary*

66. Bill is the proprietor of a medium sized insurance broking firm. He operates his business entirely from an inner city office building and all appointments with clients are conducted at these premises. He does not require a motor vehicle for business purposes.

67. Bill enters into an agreement to sell his business to Jake. Under the arrangement, Bill supplies his client list, goodwill, office furniture and equipment, and assigns the lease over the premises.

68. As a motor vehicle is not one of the things that is essential for the continued operation of Bill's enterprise, it is not necessary for Bill

[11] *Pine v. CIR* (1998) 18 NZTC 13 570; *Belton v. CIR* (1997) 18 NZTC 13 403; *Allen Yacht Charters Ltd v. CIR* (1994) 16 NZTC 11 270.

to supply a motor vehicle to Jake as part of the arrangement. That is, it is not one of the things that must necessarily be supplied under the arrangement for it to qualify as a 'supply of a going concern'.

*Example: Things that are necessary*

69. Ben conducts a mobile mechanic business. He has a specially fitted out van which carries all his tools and equipment. Ben travels widely throughout the metropolitan area and carries out repairs at clients' premises. He does not have a workshop of his own where repairs can be performed.

70. Ben enters into an agreement with Pistons Pty Ltd ('Pistons'), a company that owns several motor repair workshops, to sell his business. Under the arrangement between Ben and Pistons, Ben supplies his client list, the mobile telephone number, goodwill and motor vehicle, together with all the equipment and tools.

71. Ben's motor vehicle is essential to the continued operation of his enterprise and is one of the things that must necessarily be supplied under the arrangement for it to qualify as a 'supply of a going concern'.

### *Premises*

72. Where a particular enterprise is necessarily conducted from premises and the supplier wishes to make a 'supply of a going concern', then either the premises, or the right to occupy the premises, must be supplied as part of those things necessary for the continued operation of the enterprise.

73. Because a large part of the goodwill of an enterprise may be attributable to a key site, when premises occupy such a key site the particular premises must be supplied as part of the things necessary for the continued operation of an enterprise.

74. Goodwill attaching to premises on a particular site is one of the factors which will determine whether those particular premises are one of the things necessary for the continued operation of an enterprise.

75. Other characteristics or attributes of particular premises may also be determinative of the necessity for that particular premises to be supplied. For example, a factory building may have specially modified floors to take the weight of certain necessary machinery. Although little goodwill may attach to the premises, the characteristics of the building itself are such that those particular premises are necessary for the continued operation of the enterprise.

76. In other circumstances where premises are essential for the continued operation of an enterprise, the supply of **particular** premises may not be necessary for the continued operation of the enterprise. The supply of alternative suitable premises by the supplier in such a case is the supply of that thing which is necessary, that is, premises.

77. However, where premises are necessary for the continued conduct of the enterprise and premises are not supplied by the supplier because the recipient has suitable premises available prior to the day of the supply, the supplier is not supplying a thing which is necessary for the continued operation of an enterprise.

78. In limited circumstances, premises are not one of the things necessary for the continued operation of the enterprise. This is the case where an enterprise requires few tangible assets, for example, a personal fitness trainer who visits clients and does not need premises of his own.

*Example: Premises that are not necessary*

79. Betty is a clairvoyant who works from home. Betty provides tarot readings over the telephone using a 0055 number. Betty sells her business including her cards, the files on her regular clients, her advertising material, her trading name "Madame Ecarte" and the 0055 number to Bruce. She is not required to supply her home as a part of the supply of a going concern. Premises are not an essential part of her enterprise.

*Example: Particular premises that are not necessary*

80. Beagles operates a flying school out of a hangar which he leases from the local airport. He decides to sell his training aircraft, business name, furniture and fittings, telephone number, etc., to Red Barron Pty Ltd, the proprietor of another flying school. Beagles wishes to retain the hangar which he currently leases and commence a new business of selling aircraft components. Beagles enters into a lease of a second hangar at the airport and assigns the lease to the purchaser.

81. Although premises are needed to conduct the flying school, it is not necessary to supply the same premises from which the enterprise is conducted by Beagles. The supply of alternative premises, together with the supply of the training aircraft, business name, furniture and fittings, telephone number, etc., to the recipient, is the supply of all of the things that are necessary for the continued operation of the enterprise.

*Example: Particular premises that are necessary*

82. Deli Co. conducts a delicatessen business from leased premises adjacent to a large grocery retailer within a suburban shopping mall. Deli Co. negotiates the sale of the business to another registered entity, New Co., which has its own premises from which it intends to operate the delicatessen. The contract provides that the business name, plant and equipment, stock and goodwill are to be supplied to New Co. Deli Co. retains its premises and intends to commence another business from these premises.

83. Because the delicatessen is conducted from a key site within the mall, the particular premises are necessary for the conduct of the delicatessen business. The supply is not the 'supply of a going concern' as Deli Co is not supplying all of the things that are necessary for the continued operation of the supplier's enterprise.

### *Things brought into existence at the time of the supply*

84. The supply of all of the things that are necessary for the continued operation of an enterprise may require that the supplier enters into contracts, leases or other things which were not in existence prior to the supply. This will be the case where the supplier retains the ownership of premises from which an enterprise is conducted, but supplies the business structure and possession of the property by way of a lease.

*Example: Contracts entered into at the time of the supply*

85. Sunset Unit Trust owns and operates a nursing home on a particular site. Hands On Pty Ltd ('Hands On') enters into a contract to purchase the business of operating the nursing home. Plant and equipment, residents' records and stock are supplied as part of the arrangement. Permission was sought and granted by the relevant authority to transfer the bed allocation and a lease agreement was drawn up with Hands On to become effective on the day of settlement.

86. As the premises that are necessary for the continued operation of the enterprise were supplied by way of lease, all of the things that are necessary for the continued operation of an enterprise were supplied by the supplier.

### *Statutory licences, permits, quotas or similar statutory authorisations*

87. The supply of all of the things that are necessary for the continued operation of an enterprise that has or is required to have, as part of its business activities, statutory licences, permits, quotas or

similar things, other than personal qualifications discussed in paragraph 113 below, must include those things as part of the supply in order for it to be the 'supply of a going concern'.

88. Some enterprises are required by law to be operated under a licence, permit or other statutory authorisation. Examples of this are liquor licences and fishing licences. Some industries also have statutory allocations or quotas, such as water allocations or sugar quotas.

89. Where a supplier is permitted by the relevant statutory regime to transfer the licence, permit or other statutory authorisation, it must transfer it. Where the supplier may only transfer the thing with permission from a relevant entity, it must attempt to gain that permission. As discussed in paragraph 45 above, where the supplier, having made all reasonable attempts to transfer the thing, has no option but to surrender it in favour of the recipient, the surrender and reissue will be, in substance, a supply of the licence, permit or other statutory authorisation by the supplier.

90. Where the statutory permissive licence is necessary for the continued operation of an enterprise and a new licence is not in fact issued to the recipient in consequence of the surrender by the supplier of an existing licence, the supplier has not provided that thing to the recipient regardless of whether the supplier has used best endeavours to procure the intended result. The supply of all other things that are necessary for the continued operation of an enterprise will not satisfy the requirement in paragraph 38-325(2)(a). In these circumstances, the supply was not in fact a GST-free supply. The supplier will have a liability to pay GST.

### *Supply by a lessor of the benefits of covenants under a lease*

91. The owner of an enterprise which consists solely of the leasing of property cannot make a 'supply of a going concern' when supplying the real property subject to the lease to the lessee. All of the things that are necessary for the continued operation of the enterprise includes the supply of the property and the covenants. The owner is not able to supply to the lessee the benefit of the covenants which are necessary for the continued operation of the existing enterprise of leasing the property.

92. In the decision of the New Zealand Court of Appeal in *Pine v. CIR* (1998) 18 NZTC 13,570, the majority of the Court held that the supplier could supply the interest in the real property subject to a lease to the tenant as a going concern. The decision of the court turned largely on a consideration of the doctrine of merger, the court concluding that the merger of the interests in the land did not occur until after the point of supply. The ability of the supplier to supply the

benefit of the covenants under a lease was not considered by the court. The decision in *Pine v. CIR* has no application to the issue of whether the benefit of covenants can be passed on to the recipient of a supply of freehold premises where the recipient is a lessee under an existing lease.

### *Goodwill*

93. Goodwill is intangible property. It attaches to a business[12] and cannot attach to an enterprise which is not a business.

94. The supply of goodwill is not a conclusive factor in determining whether a supply under an arrangement is the 'supply of a going concern'.[13] However, when an 'identified enterprise' has goodwill which is capable of being supplied, that goodwill[14] must be supplied as one of the things that are necessary for the continued operation of that enterprise.

95. In *CIR v. AGH Finance Ltd* (1985) 7 NZTC 5010, Coke J said:

> 'At best the question whether any goodwill changed hands can only be one factor in deciding whether or not an existing business was purchased or acquired.
>
> ...Where a business has undoubted goodwill but only the assets are bought, with an exclusion of goodwill and items (such as trade names and existing contracts) usually associated with goodwill, it is likely to be easy to conclude that the business itself has not been acquired.'

96. In the case of goodwill arising from the personal attributes of an individual, it will be sufficient compliance with the requirement that goodwill is supplied for the supplier to agree to introduce existing customers to the recipient.

*Example: Goodwill arising from personal attributes*

97. Enrico's Coffee Emporium is well known not only for the quality of the coffee beans sold there, but also for Enrico's friendliness and knowledge of coffee. A large number of his clients travel some distance to purchase coffee from his store and to discuss the rival merits of various blends with him. Enrico intends to retire and sells the store complete with all stock, fixtures, plant, etc., to Julius. Much of the goodwill of the business is personal goodwill and

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[12] *IR Commrs v. Muller & Co.'s Margarine Ltd* [1901] AC 217; *FC of T v. Murry* (1998) 39 ATR 129; Taxation Ruling TR 1999/16

[13] *Kenmir Ltd v. Frizzell* [1968] 1 WLR 329.

[14] *FC of T v. Murry* (1998) 39 ATR 129; (1998) 193 CLR 605; 98 ATC 4585.

Enrico undertakes to remain after the sale for a period during which he will provide training to Julius and also introduce him to his clientele.

98. Enrico will have complied with the requirement to supply the goodwill of the business as part of all of the things that are necessary for the continued operation of the coffee emporium.

### *Restrictive Covenants*

99. Some arrangements for the supply of a business may include restrictive covenants. The supply of a restrictive covenant by the supplier is one of those things that are necessary for the continued operation of an enterprise in circumstances where one is supplied. Failure to supply a restrictive covenant as part of the arrangement, however, will not mean that one of the things that is necessary for the continued operation of the enterprise has not been supplied. This is because the 'identified enterprise' in each case is a different enterprise, the nature of which depends upon whether a restrictive covenant is supplied. Where a restrictive covenant is provided by the supplier, the enterprise will be one against which the former proprietor is unable to compete.

### *Intellectual property*

100. Where intellectual property exists and is necessary for the continued operation of the enterprise which is the subject of the supply, the supply of things not including the intellectual property is not the 'supply of a going concern'.

### *Franchises*

101. A franchisee cannot supply its franchise as a going concern to another entity which is to become the franchisee, unless the franchisee is capable of supplying all of the things that are necessary for the continued operation of the enterprise. In many instances, restrictions are imposed under the franchise agreement on the ability of the franchisee to transfer or assign the benefit of the franchise agreement.

102. The benefit of a franchise agreement is a thing which is necessary for the continued operation of an enterprise. Where, under the terms of the franchise agreement, the franchisee can supply the franchise agreement to an incoming franchisee, it must be supplied. If the agreement can only be supplied subject to the franchisor's approval, the franchisee must seek approval and, if such approval is given, transfer the agreement.

103. As discussed at paragraph 45 above, if either the franchise agreement does not allow the transfer of the agreement to the recipient or permission to transfer the agreement is withheld by the franchisor, surrender of the rights under the agreement in favour of the recipient will be the supply of the agreement, provided a new agreement is entered into by the franchisor and the recipient on similar terms.

*Example: Supply of a franchise without franchise agreement*

104. Outgoing Ltd ('Outgoing') is carrying on a franchised cleaning business. It does not operate from premises, but has plant and equipment, contracts with the entities for which it supplies cleaning services, and a franchise agreement with the franchisor. The head franchise agreement requires any prospective purchaser of the business to enter into a new franchise agreement.

105. Outgoing enters into a contract of sale which includes the assets of the business and the service contracts with clients with Incoming Ltd ('Incoming'). Outgoing is unable, because of the terms of the agreement, to supply the franchise agreement by transfer. Outgoing surrenders its rights under the franchise agreement in favour of Incoming. The franchisor enters into a new agreement with Incoming on substantially similar terms as the previous agreement.

106. Outgoing has supplied the benefit of the franchise agreement by the surrender of its rights under the agreement and securing the entry into a new franchise agreement between the franchisor and Incoming.

### *Staff*

107. Employees are not 'things' as defined in section 195-1 and therefore are not of themselves 'things that are necessary for the continued operation of an enterprise'. However, the benefit of a contract of employment or service is a thing which may be a thing 'necessary for the continued operation of an enterprise'. As a matter of law, employment contracts are personal contracts and are incapable of assignment.[15] Strict application of this legal principle would lead to a conclusion which would preclude the supply of employees of an enterprise as one of the things necessary for the continued operation of the enterprise.

108. In commercial practice, the retention of employees may be facilitated upon a change in ownership of the business or undertaking in various ways. Provided that the supplier takes all reasonable steps which are commercially necessary to facilitate the continued

[15] *Nokes v. Doncaster Amalgamated Collieries Ltd* [1940] AC 1014.

employment of necessary employees in the enterprise after the day of the supply, the requirement that the benefit of the employment service contracts as a thing that is necessary for the continued operation of the enterprise be supplied by the supplier will be satisfied.

109. The services of employees are necessary for the operation of many enterprises. In the case of a key employee, the benefit of a contract of employment covering the key employee is the thing which is necessary for the continued operation of the enterprise.

110. In the case of larger enterprises, a particular number of employees will be necessary for the continued operation of the enterprise. In such a case, the parties must:

(a) determine the number of employees which are necessary for the continued operation of the enterprise; and

(b) secure the benefit of contracts of employment relating to the required workforce in the manner described above.

*Example: Key personnel*

111. Geordie is a computer programmer with GoingCom Ltd ('GoingCom'), an entity that conducts a software business. Geordie developed GoingCom's best selling product, a virus checker, and is the only person who is capable of updating the software for new viruses, debugging it and providing technical support in relation to that product as part of GoingCom's after sale service. GoingCom agrees to sell its entire business to DigiConcern Pty Ltd ('DigiConcern') as a going concern.

112. Because the services of Geordie are essential to the continued operation of the enterprise, the agreement by Geordie to continue to work with the software business under DigiConcern must be secured to enable the supply by GoingCom to be the 'supply of a going concern'.

113. The services of a sole proprietor are not provided pursuant to a contract and therefore are not a thing that is necessary for the continued operation of the enterprise. Similarly, where the nature of the business is such that personal qualifications (e.g., educational qualifications, practicing certificates, etc.) attaching to an individual are necessary for the continued conduct of the business, we consider that the supply of those attributes would require the supply of the individual. However, as the individual is not a 'thing', because an individual is not capable of being supplied, the supply of an individual with such attributes is not required under paragraph 38-325(2)(a).

*Example: Personal qualifications*

114. Marco, a health practitioner, supplies his practice to another practitioner. Marco is required to hold a practising certificate which he gained through study and supervised practice. The qualification is personal to Marco and cannot be transferred to another entity. Provided that everything else necessary to continue to operate the practice is supplied, including the client list, this may be the 'supply of a going concern'.

### Supply of parts of an existing enterprise to two or more recipients

115. Paragraph 38-325(2)(b) expressly recognises that each supply under the relevant arrangement of all of the things that are necessary for the continued operation of part of a larger enterprise may be the 'supply of a going concern'. Equally, supplies of all of the things that are necessary for the continued operation of parts of a larger enterprise may be separate supplies of going concerns to two or more recipients provided the two different parts of the enterprise are each capable of separate independent operation.

116. Where the owner of both a business enterprise and of the real property upon which the business enterprise is necessarily conducted sells the business part of the enterprise to a second entity and the business premises to a third entity, the supply to the second entity will not be the 'supply of a going concern' because that entity has not been supplied with one of the things necessary for the continued operation of that enterprise, that is, the business premises. However, where the owner of both the business enterprise and the premises grants a lease of the premises in favour of the second entity immediately before making the supply to that second entity, the supplier is supplying the second entity with all of the things that are necessary for the continued operation of the enterprise, notwithstanding a subsequent supply of the real property subject to a lease to the third entity.

117. Similarly, the supply of the real property to the third entity subject to a lease to a second entity in the circumstances described in the preceding paragraph, may also be the 'supply of a going concern' because an enterprise of leasing the relevant property is conducted by the supplier up to the day of the supply, albeit for a brief period of time. The entity, being the owner of both the business and the real property, is making two supplies, each of which is capable of being the 'supply of a going concern'.

### Supplier carries on the enterprise until the day of the supply

118. A supply under an arrangement will only be the 'supply of a going concern' where the enterprise is carried on by the supplier until

the day of the supply. All of the activities of the enterprise must be active and operating on the day of the supply. The activities must be capable of continuing after the transfer to new ownership.

119. A supply will not be a 'supply of a going concern' when, on the day of the supply, the activity carried on by the enterprise has ceased. The New Zealand case of *Belton v. CIR* (1997) 18 NZTC 13,403 provides a useful illustration of a failure to fulfil a similar requirement under the New Zealand law. There, an owner of an operating motel sold the motel. Under the contractual agreement, the sale was subject to vacant possession and the land, building and chattels only were transferred to the purchaser. At settlement, the motel had been closed down and there were no future bookings. After the settlement date, the premises did not immediately operate as a motel but did so again several weeks later.

120. The Court accepted that the vendor had supplied all the assets necessary for the supply of the motel as a going concern:

> 'The fact that the purchaser could resume operations shortly after the transfer illustrates that there was available a business structure as well as the business activity. Mr Belton could exploit the location goodwill and the benefits flowing from pre-existing clientele, advertising and background. At settlement he was in a position to resume the operation of the motel business notwithstanding the vacant possession which he demanded and received.'

121. However, the supply was held not to be of a going concern because, at the time of the supply, the motel business was not operating.

122. A supplier, who temporarily ceases some activities of an enterprise for a short period to facilitate the supply under the arrangement, has not ceased to carry on the enterprise for the purposes of paragraph 38-325(2)(a).

123. The enterprise must be carried on by the supplier which may do so itself or have another entity carry on the enterprise on its behalf. However, an entity that does not have legal ownership or possession of the enterprise is not in a position to deal with that enterprise and therefore cannot be the supplier of all of the things necessary to continue to operate the enterprise.

*Example: Enterprise not carried on at the day of the supply*

124. Old Salt Limited ('Old Salt') owns a fishing vessel and fishing licence, both of which it leases to the Rockhopper partnership on a month to month basis. The partnership carries on a business of fishing using the trawler and licence. Old Salt enters into a contract to sell the

fishing boat and licence to George Gudgeon, terminating the lease arrangement with Rockhopper two days before the settlement date. Old Salt did not carry on the enterprise of leasing the trawler and licence up to the day of the supply and therefore cannot make a 'supply of a going concern'.

### Continued operation

125. The term 'carrying on an enterprise' includes doing anything in the course of the commencement or termination of the enterprise.[16] A supplier may carry on an enterprise to the day of the supply for the purposes of paragraph 38-325(2)(b) during the period of commencement or termination of an enterprise.

126. A supplier is unable to supply all of the things that are necessary for the continued operation of an enterprise unless the relevant enterprise is not only being 'carried on', but is also operating. Where an enterprise engaged in an activity ceases to carry on that activity and the assets are in the course of being sold off, the enterprise is being 'carried on', but is not operating.

*Example: Partly tenanted building*

127. The Bullish Unit Trust enters into a contract to sell a large commercial building which it has leased out for several years. At the time of sale, the building has only one tenant which occupies 10% of the available floor space. The balance of the floor space is available for lease and the trust has engaged a leasing agent to find tenants for the remaining area. The trust is carrying on an enterprise of leasing the building as it is carrying on leasing activities on a regular or continuous basis.

128. The activity of leasing a building which has previously been leased to a tenant remains an 'enterprise' of leasing for the purposes of section 9-20 of the GST Act during the period of temporary vacancy when a new tenant is being actively sought by the building owner. However, where a building has not previously been leased to a tenant, an 'enterprise' is not operating until the activity of leasing is actually commenced.

129. In the course of conducting an enterprise of leasing a building, certain floors may be unavailable for lease temporarily while repairs, refurbishments or other activities requiring vacancy take place. The requirement that vacant floors be actively marketed will not apply to those floors for the period during which the activities are taking place.

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[16] Section 195-1.

130. Some areas or floors may not be available for lease but may still be part of the enterprise of leasing the building. The areas may be used for storage of cleaning equipment, as offices for the building manager or for some other purpose relevant to the enterprise of leasing. Provided that the entity can demonstrate that all of the floor space in the building is part of an enterprise of leasing at the time of the supply, the supply of the whole building may be the 'supply of a going concern'.

*Example: Floors not actively marketed*

131. Bearish Pty Ltd enters into a contract to sell a large commercial building which it has leased out for a number of years. At the time of sale, the building has only one tenant which occupies 10% of the available floor space. A number of floors are available for lease and the company has engaged a leasing agent to find tenants for those floors. As a result of a policy of refurbishment of floors on the termination of a tenancy on those floors, the remaining floors are neither tenanted nor being actively marketed.

132. The company is carrying on an enterprise of leasing the building as it is carrying on leasing activities on a regular or continuous basis. The refurbishment of the vacant floors is one of the activities of the enterprise of leasing the building.

133. Where all of the things that are necessary for the continued operation of the same enterprise are supplied two or more times in succession, each of the supplies subsequent to the initial supply as a going concern cannot be the 'supply of a going concern' unless the relevant supplier of that supply has actually operated the enterprise and carries on the enterprise until the day of the supply which it makes.

134. The recipient of a 'supply of a going concern' that immediately on-sells the things that are necessary for the continued operation of the enterprise to a subsequent purchaser without actually operating the enterprise cannot satisfy the requirement in subsection 38-325(2) that it carry on the enterprise to the day of the supply. If, however, the operation of the enterprise continues uninterrupted throughout the subsequent supply(s), each supplier will be capable of satisfying the subsection.

**The day of the supply**

135. The day of the supply is determined in each case by reference to the terms of the particular contract, if applicable, and the nature of the supply. It is the date on which the recipient assumes effective control and possession of the enterprise which is carried on by the

supplier. The day of the supply occurs when the supplier has done everything to satisfy the obligations under the contract or arrangement governing the supply and the recipient has assumed effective control and possession of all of the things that are necessary for the continued operation of the enterprise.

*Example: No change in effective control*

136. On 1 August 2000, Frank enters into negotiations to buy a manufacturing business from Kerry. Negotiations are concluded on 31 August and contracts are exchanged on that date with settlement occurring on 31 October 2000. Kerry continues to conduct the business until 31 October. The contract provides that the transfer of the assets and undertaking of the business is deemed to have occurred at midnight on 31 August and that profits or losses incurred after that date are those of the purchaser.

137. The day of the supply in these circumstances is the date on which effective control actually passes, that is, 31 October 2000. Notwithstanding that the economic risk and benefit are deemed to have passed at an earlier date, effective control did not pass until 31 October.

*Example: Change in effective control*

138. Sue enters into a contract to purchase a whale watching business from Cheryl. The assets of the business include a boat, goodwill and a statutory permissive licence from the State Government. Sue takes possession of the boat on 31 October 2000 and commences to carry on the business from that date. The transfer of the licence is subject to formal consent from the relevant Minister and this process is not completed until 30 November. Under the contract, Cheryl is required to work in the business until the transfer of the licence to Sue has been completed.

139. The day of the supply is 31 October 2000 because economic ownership and effective control of the enterprise has actually passed to Sue on that day, notwithstanding the delay in supply of one of the things necessary for the continued operation of the enterprise.

**Supply of things in addition to those necessary for the continued operation of an enterprise**

140. Supplies made under an arrangement, under which all of the things that are necessary for the continued operation of the 'identified enterprise' are supplied to the recipient, may each be the 'supply of a going concern' for the purposes of subsection 38-325(2). The

arrangement to which the provision refers is the arrangement under which all of the things that are necessary for the continued operation of an enterprise is supplied (paragraph 38-325(2)(a)). It may include the supply of those things which, while not essential to the continued operation of the business, are utilised in the enterprise carried on by the supplier until the day of the supply (paragraph 38-325(2)(b)).

141. The relevant arrangement may be narrower than the arrangement entered into by the supplier and recipient. The arrangement may include a single supply, multiple supplies or part of a supply. What the relevant arrangement is will be a question of fact in each case and will depend upon what is the 'identified enterprise'.

142. The supplies made under the relevant arrangement are those which are capable of being GST-free. Supplies which are not made under the relevant arrangement, even if made under the wider arrangement, are not GST-free as supplies of going concerns.

143. If part of a supply is under the relevant arrangement and part is not, section 9-80 provides a method of apportionment of the GST-free part and the taxable part.

*Example: Supply of things not under the relevant arrangement*

144. A motor mechanic contracts to sell his motor repair business, including the building from which it operates, and a residence located on an adjoining block in which he lives. The supply of the business and any related buildings is a supply under the relevant arrangement. The supply of the residential premises is neither the supply of a thing which is necessary to the continued operation of the 'identified enterprise', nor the supply of a thing used in carrying on the enterprise until the day of the supply. It is not a supply under the relevant arrangement.

145. When all of the shares constituting the issued capital of a company are supplied under an arrangement, whether or not the supply of the shares will be under a relevant arrangement will be a question of fact. If the shares are utilised in carrying on the 'identified enterprise', then they may be supplied under the relevant arrangement. However, where shares are not utilised in the enterprise carried on or are passive investments, they will not be capable of being supplied under the relevant arrangement.

146. The supply of a bundle of shares which does not constitute the whole of the issued capital of a company will only be a supply of one of the things necessary for the continued operation of an enterprise, where the 'identified enterprise' is the trading of shares.

*Example: Supply of shares in a subsidiary company*

147. XYZ Ltd ('XYZ') is a parent company for the XYZ group of companies which are engaged in an office furniture manufacturing business. The manufacturing premises are owned by XYZ which conducts the business in its own right, however, a wholly owned subsidiary, Subco Ltd ('Subco'), owns all plant and equipment used by XYZ pursuant to various lease arrangements. XYZ enters into an agreement to sell the manufacturing business to ABC Ltd. Under the contract, XYZ agrees to sell all assets associated with the business, including shares held in Subco.

148. The right to use plant and equipment pursuant to the lease arrangements is a thing necessary for the continued operation of the manufacturing business. The supplier may supply that thing by either:

(a) retaining the shares and continuing the lease arrangements; or

(b) selling the shares under the arrangement.

*Example: Shares as a passive investment*

149. Sparky Pty Ltd ('Sparky') owns a small electrical repairs business which it operates from rented premises. It enters into an arrangement with Ampere Ltd under which Sparky will supply the stock on hand, work-in-progress, advertising material, signage and the lease of the premises. The supply under the contract also includes three parcels of shares in blue chip companies from which Sparky derives dividend income.

150. The part of the supply which relates to the parcels of shares will not be under the relevant arrangement as not only are the shares not necessary for the continued operation of the enterprise, but the shares are not used in carrying on the enterprise until the day of the supply.

## Agreed in writing

151. One of the requirements of section 38-325 is that the supplier and the recipient have agreed in writing that the supply is of a going concern. This agreement need not necessarily form part of the arrangement under which the relevant supply is made.

152. The GST Act does not specify what form the agreement has to be in, nor does it define the term 'agreed in writing'. The term 'agreed' means 'to be in one mind; harmonise in opinion or feeling'.[17]

[17] Macquarie Dictionary (1997; 3rd edition).

153. Section 25 of the *Acts Interpretation Act 1901* defines 'writing' as 'includes any mode of representing or reproducing words, figures, drawings or symbols in a visible form.' In *Peverill v. Meir* (1990) 95 ALR 401, Justice Burchett concluded that:

> 'When the Act requires the request to be in writing, I think it refers to a request which read reasonably, conveys the information that the procedure in question is to be performed.'

154. The term 'agreed in writing' means that the supplier and the recipient have made a mutual declaration in such form that clearly evidences that they agree that the supply is a 'supply of a going concern'.

155. The supplier and the recipient must agree that the supply is a 'supply of a going concern' on or before the time of the supply.

156. An agreement in writing by the parties that the supply is a 'supply of a going concern' will not conclusively determine that the supply is a 'supply of a going concern' where the other requirements of Subdivision 38-J are not satisfied. This will depend on a consideration of all factual circumstances. For example, a supply which does not include all of the things that are necessary for the continued operation of an enterprise will not be a 'supply of a going concern' under Subdivision 38-J, notwithstanding the terms of any agreement between the parties that the supply is a 'supply of a going concern'.

157. Similarly, a supply to a recipient who is not registered or required to be registered[18] will not be a GST-free supply, notwithstanding the terms of any agreement between the parties that the supply is a 'supply of a going concern'.

### Recipient is registered or required to be registered

158. Paragraph 38-325(1)(b) requires that the recipient is registered or is required to be registered. A recipient that is required to be registered in respect of the enterprise on and from the date of the supply will satisfy the requirement in paragraph 38-325(1)(b). If the recipient is not required to be registered, but chooses to register to obtain the benefit of the provision, the mere lodging of an application to be registered will not satisfy the requirements of paragraph 38-325(1)(b). The effective date of registration of the recipient must be on or before the day of the supply.

[18] Division 23.

### Options to acquire a thing or things as a going concern

159. Subsection 9-30(1) deals with supplies that are GST-free. In addition to those supplies which are GST-free under Division 38 of the GST Act, including the 'supply of a going concern', the subsection also provides that the supply of a right to receive a supply that would be GST-free under Division 38 is GST-free.

160. The supply of an option to acquire a supply of a going concern is a supply of a right to receive the 'supply of a going concern'. Whether the supply of the option is GST-free will depend upon the wording of the option. The wording must have the effect that the supply made on the exercise of the option is GST-free, or the option will not be exercised. For example, an option to acquire a load of apples is not GST-free, but an option to acquire a load of apples fit for human consumption is.

161. When this principle is applied to the option to acquire a 'supply of a going concern', the parties to the option must agree that, on the exercise of the option, the supply will be GST-free. The parties must specify that, on the exercise of the option, what is supplied will satisfy the conditions of section 38-325.

### Going concerns and partnerships

162. A partnership interest is the property of the partner and may be assigned or sold by the partner. In the case of a common law partnership, any dealing with the partnership interest, other than by assignment, terminates the partnership. The Partnership Act allows the partners to agree in the partnership agreement that the partnership continues after a change in the partners.

163. If such an agreement is in place, merely admitting new partners has no effect and cannot be the 'supply of a going concern'. What has happened is that a partnership interest has been created. The supply of an interest by assignment is not the 'supply of a going concern' as the enterprise is not being carried on by the partner. The supply of an interest by sale will also not be a 'supply of a going concern' as the enterprise is not being carried on by the partner. Further, the supply is not a supply under an arrangement under which all of the things that are necessary to continue to operate the enterprise carried on by the partnership are supplied.

164. Where the partnership entity sells all of its assets to another entity (including a partnership constituted of some of the original partners) and that entity is registered or required to be registered, the supply may be GST-free as a 'supply of a going concern'. Similarly, where the partnership sells part of its enterprise to another entity and all of the conditions of section 38-325 are satisfied, the supply may be GST-free as the 'supply of a going concern'.

### Going concerns and companies

165. The supply of all of the shares in a company that conducts an enterprise is not the 'supply of a going concern' when the shares are all that is supplied. The supply of the shares may satisfy the test in paragraph 38-325(2)(a) as it is the supply of all of the things that are necessary for the continued operation of an enterprise. The supplier of the shares is the shareholder. The supply will fail the test in paragraph 38-325(2)(b) because the supplier of the shares does not conduct the enterprise and so cannot carry it on until the day of the supply. The 'identified enterprise' is the enterprise conducted by the entity which is the company. A supply of shares may be a financial supply.[19]

166. However, where an entity which conducts an enterprise is a company and the company supplies all of the things that are necessary for the continued operation of the enterprise in accordance with the conditions of Subdivision 38-J, each supply is a GST-free 'supply of a going concern'.

### Going concerns and trusts

167. An enterprise may be conducted by an entity which is a trust. It is the trustee of the trust, as the entity conducting the enterprise, which may make a 'supply of a going concern'.

### A 'supply of a going concern' which would otherwise be input taxed

168. Where a supply under an arrangement is GST-free because of the application of Subdivision 38-J, input tax credits on creditable acquisitions made in relation to the supply are available to the supplier.

169. Input tax credits relating to a supply, which would have otherwise been input taxed but is GST-free because of the operation of the Subdivision, are available to the extent that they relate to the supply under the arrangement. This means that input tax credits relating to the acquisition and use of the thing supplied will not be available, but those relating to the supply of the thing under the arrangement are available.

170. The acquisition of a thing used to make input taxed supplies is not a creditable acquisition to the extent that it is used for that purpose. Input tax credits are also not available in relation to the use of the thing to make input taxed supplies. However, as the supply of the thing under an arrangement which satisfies the conditions of

[19] Subregulation 40-5.09(3) Item 10 of A New Tax System (Goods and Services Tax) Regulations 1999.

Subdivision 38-J is GST-free, acquisitions for the purposes of making that supply are for a creditable purpose and the input tax credits which relate to those acquisitions will be available to the supplier.

*Example: Availability of input tax credits*

171. Gerald acquires a block of flats which are subsequently let as residential premises for several years. Gerald sells the property to Grace with existing leases intact. The supply is for consideration, Gerald and Grace are both registered for GST and they agree in writing that the supply is of a going concern. In the course of the sale, Gerald consults a solicitor and utilises the services of a real estate agent.

172. As the acquisition of the premises by Gerald is for the purpose of making input taxed supplies, it is not acquired for a creditable purpose and input tax credits are not available in relation to the acquisition. The acquisitions made in the course of the leasing activities, such as plumbing and painting, are also not acquisitions for a creditable purpose. The input tax credits in relation to these acquisitions are not available to Gerald.

173. The supply of the premises as a going concern is GST-free and acquisitions made in the course of making that supply are made for a creditable purpose. The input tax credits in relation to the acquisition of legal services and real estate services are available to Gerald.

**Mortgagee exercising a power to dispose of a debtor's property**

174. A supply of property by a mortgagee is a taxable supply if the supply would have been a taxable supply had it been made by the debtor.[20]

175. A supply is a GST-free 'supply of a going concern' by a mortgagee if the requirements of subsection 38-325(2) are met by the mortgagee in their own capacity as the supplier.

176. Where a mortgagee is empowered to sell some, but not all, of the assets of an enterprise that are necessary for the continued operation of an enterprise, the supply will not satisfy paragraph 38-325(2)(a).

177. Where a mortgagee is empowered to sell the assets of an enterprise, but has no power to enter into possession and conduct the activity of the enterprise, the supply will not satisfy the requirement in paragraph 38-325(2)(b) that the supplier carry on the enterprise until the day of the supply.

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[20] Section 105-5.

178. Subsection 105-5(3) provides that a supply is not a taxable supply where the debtor advises you in writing or, in the absence of a written statement, you conclude on the basis of reasonable information, that the supply would not have been a taxable supply if it had been made by the debtor. The subsection will have no application in relation to section 38-325 where a supply is made by a mortgagee in possession as the requirements of the section cannot be satisfied by the debtor. Specifically, the debtor cannot carry on the enterprise until the day of the supply and, consequently, the relevant notice cannot be given.

# Detailed contents list

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# Your comments

180. If you wish to comment on this draft Ruling, please send your comments promptly by 11 April 2001 to:

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**Commissioner of Taxation**
28 February 2001

*Previous draft:*
Not previously issued in draft form

*Related Rulings/Determinations:*
GSTD 2000/8; MT 2000/1;
TR 1999/16

*Subject references:*
- adjustments
- agreed in writing
- arrangement
- consideration
- continued operation
- day of the supply
- enterprise
- franchises
- going concern
- goodwill
- goods and services tax
- GST-free
- increasing adjustment
- input tax credits

- input taxed supply
- leases
- mortgagee
- options
- premises
- restrictive covenants
- shares
- statutory licence
- supply of a going concern
- taxable supply

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ATO references:
NO 2000/019536
BO
ISSN: 1443-5160