GSTR 2005/D3 - Goods and services tax: the application of A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination MSV 2005/3 to real property acquired or held before 1 July 2000

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Draft Goods and Services Tax Ruling

Goods and services tax: the application of *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination MSV 2005/3* to real property acquired or held before 1 July 2000

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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 taxpayers and practitioners, as it is not a ruling or advice for the purposes of section 37 of the ***Taxation Administration Act 1953****. The final Ruling will be a public ruling for the purposes of section 37 and may be relied upon by any entity to which it applies.*

What this Ruling is about

1. This Ruling explains how the *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination MSV 2005/3* (the determination) applies to a freehold interest, stratum unit,[1] or long-term lease[2] (referred to in this Ruling collectively as 'real property') that was acquired or held before 1 July 2000.

2. A copy of the determination is attached at Schedule 1. This determination was made under section 75-35 of the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act).

[1] 'Stratum unit' is defined in section 195-1 as having 'the meaning given by subsection 124-190(3) of the *Income Tax Assessment Act 1997*. Subsection 124-190(3) defines a stratum unit as 'a lot or unit (however described in an Australian law or a foreign law relating to strata title or similar title) and any accompanying common property'.

[2] 'Long-term lease' is defined in section 195-1 as 'a supply by way of lease, hire or licence (including a renewal or extension of a lease, hire or licence) for at least 50 years if:
(a) at the time of the lease, hire or licence, or the renewal or extension of the lease, hire or licence, it was reasonable to expect that it would continue for at least 50 years; and
(b) unless the supplier is an *Australian government agency – the terms of the lease, hire or licence, or the renewal or extension of the lease, hire or licence, as they apply to the *recipient are substantially the same as those under which the supplier held the premises.'

3. Section 75-35 of the GST Act provides for the Commissioner to determine, in writing, the requirements for making valuations for the purposes of Division 75 and that a valuation made in accordance with these requirements is an approved valuation.

4. The determination is about the requirements for making an approved valuation of real property.

5. The determination applies to taxable supplies of real property made on or after 1 December 2005. It is a legislative instrument and has the force of law. Unlike public rulings which are binding only on the Commissioner, the determination is binding on both the Commissioner and suppliers.

6. The Ruling explains in particular:

(a) how valuations are to be made under the determination made by the Commissioner (paragraphs 68 to 92);

(b) what documentation is required by a profeesional valuer to satisfy the determination (paragraph 85); and

(c) when valuations are required to be made under Division 75 the GST Act (paragraphs 69 to 72).

7. The Ruling also discusses:

(a) when you can apply the margin scheme (paragraphs 26 to 38);

(b) when you supply or acquire or hold an interest, unit or lease (paragraphs 44 to 47);

(c) how the margin for a supply is calculated (paragraphs 48 to 49);

(d) the margin for the supply of real property acquired from a deceased estate (paragraphs 50 to 56);

(e) the margin for the supply of real property acquired from an associate (paragraphs 57 to 60);

(f) whether the consideration for a supply or an acquisition includes settlement adjustments (paragraphs 61 to 67);

(g) the meaning of ‘Commonwealth, a State or a Territory’ for the purposes of items 2A and 4 in the table in subsection 75-10(3) (paragraphs 92 to 99);

(h) the meaning of ‘land on which there are no improvements’ and ‘no improvements on the land’ for the purposes of the table in subsection 75-10(3) and subsection 75-10(3A) (paragraphs 105 to 123);

(i) how the margin scheme applies to mixed supplies (paragraphs 124 to 128);

(j) increasing adjustments if part of your acquisition was ineligible for the margin scheme (paragraphs 129 to 152);

(k) working out the margin if not all the consideration has been paid (paragraphs 153 to 156);

(l) entitlement to input tax credits (paragraph 158);

(m) tax invoices (paragraph 159); and

(n) record keeping requirements (paragraph 160).

8. This Ruling does not deal in detail with subsection 75-10(2), that is, where the margin is calculated by reference to the consideration for the supplier's acquisition of the real property rather than by reference to a valuation. The consideration for the acquisition is addressed at paragraphs 50 to 69 in GSTR 2005/D4.

9. It also does not deal in detail with taxable supplies of real property made before 1 December 2005. For supplies made before 1 December 2005, see Goods and Services Tax Ruling GSTR 2000/21.[3] However, GSTR 2000/21 must be read subject to those amendments made by the *Tax Laws Amendment (2005 Measures No. 2) Act 2005* (2005 Amendment Act).

10. Unless otherwise stated, all references in this Ruling are to the GST Act.

Date of effect

11. This draft Ruling represents the preliminary, though considered, views of the Commissioner of Taxation. This draft may not be relied on by taxpayers or practitioners. When the final Ruling is officially released, it will, except for the legislative amendments made by the 2005 Amendment Act, explain the Commissioner's view of the law as it applies from 1 July 2000.

12. The legislative amendments contained in the 2005 Amendment Act apply to supplies made on or after 17 March 2005, except for the amendments to section 75-5. The amendments to section 75-5 apply to supplies on or after 29 June 2005[4] that are:

(a) made under contracts entered into on or after 29 June 2005; and

(b) are not made pursuant to rights or options granted before 29 June 2005.

13. The final Ruling will be a public ruling for the purposes of section 37 of the *Taxation Administration Act 1953* and may be relied upon, after it is issued, by any entity to which it applies. Goods and Services Tax Ruling GSTR 1999/1 explains the GST rulings system and the Commissioner's view of when you can rely on the Commissioner's interpretation of the law in GST public and private rulings.

[3] GSTR 2000/21 Goods and services tax: the margin scheme for supplies of real property held prior to 1 July 2000.
[4] The date of Royal Assent of the 2005 Amendment Act.

14. If the final public ruling conflicts with a previous private ruling that you have obtained, the public ruling prevails. However, if you have relied on a private ruling, you are protected in respect of what you have done up to the date of issue of the final public ruling.

15. If the final public ruling conflicts with an earlier public ruling (for example the Property and Construction Industry Issues Log item dealing with improvements to property) this public ruling prevails. If you have relied on an earlier public ruling, you are protected in respect of what you have done up to the date of issue of the final public ruling.

16. This means that if you have underpaid an amount of GST, you are not liable for the shortfall prior to the date of effect of the later ruling. Similarly, you are not liable to repay an amount overpaid by the Commissioner as a refund.

17. If you have relied on an earlier ruling dealing with improvements to property and the final public ruling contains an interpretation which would result in a more favourable valuation under subsection 75-10(3), you may revise your valuation to reflect this interpretation.

Background

18. If you make a taxable supply of real property, the GST payable under the basic rule in section 9-70 is 1/11th of the price.[5] However, under subsection 75-5(1), if you make a taxable supply of real property by:

- selling a freehold interest in land; or
- selling a stratum unit; or
- granting or selling a long-term lease,

you may apply the margin scheme, if you and the recipient have agreed in writing that the margin scheme is to apply.[6]

19. Under the margin scheme, the GST payable on the supply of real property is 1/11th of the margin for the supply. The margin for the supply is the amount by which the consideration for the supply exceeds the consideration[7] for the acquisition of the real property unless subsection 75-10(3)[8] or section 75-11 applies. Section 75-11 applies to supplies made on or after 17 March 2005.

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[5] Sections 9-70 and 9-75.
[6] The requirement for the agreement to be in writing does not apply if the supply falls within the former subsection 75-5(1). The former subsection 75-5(1) is addressed at paragraphs 31 to 36 and 38.
[7] Consideration is inclusive of GST, if any.
[8] Subsection 75-10(3) applies to supplies of real property acquired or held before 1 July 2000.

20. The GST payable under the margin scheme is usually lower than when the GST is worked out under the basic rule in section 9-70. Because of this, the margin scheme is used particularly if the recipient of the supply is not entitled to an input tax credit for the acquisition. The most common example is residential land or residential premises supplied to private owners for their own use or for investment purposes. However, the supplier can calculate GST under the margin scheme for supplies of all types of real property[9] including residential, commercial, retail and industrial property.

21. The Commissioner has previously issued GSTR 2000/21 which explained the *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination (No. 1) 2000* and the *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination (No. 2) 2000*. Additionally, the *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination MSV 2005/1* was made on 11 March 2005.

22. The *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination MSV 2005/3* replaces these determinations for supplies of real property made on or after 1 December 2005. GSTR 2000/21 and the legislative determinations attached to the Ruling[10] now only apply to supplies of real property made before 1 December 2005.

23. The *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination MSV 2005/3* does not replace *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination MSV 2005/2*.

24. *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination MSV 2005/2* extends the operation of the costs of completion valuation method[11] to supplies made after 1 July 2005, where the contract for the supply was entered into before that date.

25. The following summarises the major differences between GSTR 2000/21 and this Ruling:

- GSTR 2000/21 applies to supplies of real property made before 1 December 2005 where the real property was acquired or held before 1 July 2000. This Ruling only applies to taxable supplies of real property made on or after 1 December 2005 where the real property was acquired or held before 1 July 2000.

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[9] Provided the supply is a sale of a freehold interest or stratum unit or a grant or sale of a long-term lease and the other requirements of section 75-5 are met.

[10] *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination (No. 1) 2000* and the *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination (No. 2) 2000.*

[11] The costs of completion method is explained in detail in GSTR 2000/21.

- *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination (No. 1) 2000* and *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination (No. 2) 2000* now only apply to supplies made before 1 December 2005. These determinations are explained in GSTR 2000/21.
- *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination (No. 3) 2005* applies to supplies made on or after 1 December 2005.
- This Ruling also sets out the Commissioner's views on the matters referred to at paragraphs 6 and 7.

Ruling with Explanation

When can you apply the margin scheme?

26. Subsection 75-5(1) deals with applying the margin scheme. It was amended by the 2005 Amendment Act. At the same time, subsection 75-5(1A) was inserted into the GST Act.

27. Subsection 75-5(1A) and the amendment to subsection 75-5(1) apply to supplies that are:

(a) made under contracts entered into on or after 29 June 2005; and

(b) are not made pursuant to rights or options granted before 29 June 2005.

28. In all other circumstances, the former subsection 75-5(1) applies.

Subsection 75-5(1A) and the amended subsection 75-5(1)

29. Subsection 75-5(1) provides that you may use the margin scheme if the supplier and the recipient have agreed in writing that the margin scheme is to apply. Subsection 75-5(1A) provides that the agreement must be made on or before making the supply, or within such further period as the Commissioner allows.[12]

30. The decision to allow or not allow a further period within which to make an agreement is a reviewable GST decision under item 37AA in the table in subsection 62(2) of the *Taxation Administration Act 1953*.

[12] Guidelines regarding when the Commissioner will consider allowing a further period to make an agreement are set out in Practice Statement PSLA 2005/15.

The former subsection 75-5(1)

31. The former subsection 75-5(1) applies to supplies where the contract for the real property was entered into before 29 June 2005[13] or the supply was not made under a contract, for example, a transfer of real property for no consideration. Similarly, if prior to 29 June 2005, the recipient of the supply had a right or option to purchase real property, then when the right or option is exercised, the supply of this property falls within the former subsection 75-5(1).[14]

32. It provides that the supplier 'may choose to apply the margin scheme in working out the amount of GST' if the supplier makes a taxable supply of real property. It does not expressly state when the choice to use the margin scheme needs to be made.

33. However, it is the Commissioner's view that, to be entitled to apply the margin scheme under the former subsection 75-5(1) to work out the GST on a taxable supply of real property, the supplier must have chosen to apply the margin scheme at or before the time it makes the supply. If the choice is not made by that date, it is the Tax Office view that it cannot be made at a later date.

34. Support for this view is found in the wording contained in Division 75. For example, the language of subsection 75-20(1) provides that an acquisition is not a creditable acquisition if the supply was a taxable supply under the margin scheme. This suggests that the choice to apply the margin scheme must have been made by the time the taxably supply was made for the supply to be a 'taxable supply under the margin scheme'.

35. Similarly, paragraph 75-25(1)(a) refers to 'a taxable supply of real property under the margin scheme' and subsection 75-30(1) refers to 'a supply of real property under the margin scheme'. These provisions appear to be founded on the assumption that it will be known that the supply is a supply under the margin scheme, which can only be the case if the supplier has chosen to apply the margin scheme by the time the supply is made.

36. However, the Tax Office allows GST to be calculated under the former subsection 75-5(1) as if the choice to apply the margin scheme had been made by the time the supply is made in limited circumstances.[15]

Conditional application of the margin scheme

37. Commonly, contracts specify that there is no GST payable on a supply, but that if the supply is taxable then the GST payable will be calculated under the margin scheme. In these circumstances, the Commissioner accepts that the requirements in paragraph 75-5(1A)(a) have been satisfied.

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[13] The date of Royal Assent of the 2005 Amendment Act.
[14] Items 9 and 10 of Schedule 6 of the 2005 Amendment Act.
[15] See PSLA 2005/2 (GA): GST and time of choice to apply the margin scheme.

38. Similarly, where the former subsection 75-5(1) applies, the supplier has made a choice to apply the margin scheme before the supply has been made.

What is the margin for the supply?

39. The margin for the supply is the difference between the consideration for the supply and the consideration[16] for the acquisition of the real property unless subsection 75-10(3) or section 75-11 applies.

Subsection 75-10(3)

40. Subsection 75-10(3) applies if an approved valuation has been made and:

- the circumstances in section 75-11 do not apply; and
- you acquired (or in some cases held) the real property before 1 July 2000; or
- you acquired the real property on or after 1 July 2000, but the supply to you:
  - (i) was GST-free under subsection 38-445(1A); and
  - (ii) related to a supply before 1 July 2000, by way of lease, that would have been GST-free under section 38-450 had it been made on or after 1 July 2000 (item 2A).

41. Under subsection 75-10(3), the margin for the supply is the difference between the consideration for the supply and the amount determined by the approved valuation. In the context of subdivisions, if land that is part of the original broadacres is used for public purposes including roads, parklands or utilities ('lost land'), the valuation of the entire broadacres is apportioned to the total number of subdivided lots, so that the sum of the apportioned amounts equals the valuation for the broadacres (including the 'lost land').

42. When the margin scheme applies to the supply but there is no valuation, or a valuation is not an approved valuation under section 75-35, then the margin for the supply is calculated under subsection 75-10(2), provided section 75-11 does not apply.

Section 75-11

43. Section 75-11 applies if the real property was acquired from:

- a deceased estate and the deceased acquired it before 1 July 2000;[17] or

[16] Consideration in each case is inclusive of GST, if any.
[17] Section 75-11 also applies where the deceased acquired the property on or after 1 July 2000 – see paragraph 51 of this Ruling.

- an associate.[18]

When do you supply or acquire real property?

44. Most legal interests in Torrens title land are created or transferred only upon registration of the relevant instrument.

45. However, because of the practical difficulties of determining precisely when the instrument is registered that would arise if a literal interpretation of the law is to be taken, the Commissioner considers that Parliament would have intended that, in the context of GST, a less strict approach should apply.

46. For that reason, the Commissioner considers that for the sale of a freehold interest or stratum unit, the supply and the acquisition is made at settlement as this is when the purchaser (or the purchaser's agent) obtains:

- unconditional possession of a registrable instrument of transfer; or
- an instrument of transfer that would be registrable once stamped.

47. If the supply is made by way of sale or grant of a long-term lease, the lease is supplied and acquired when the recipient obtains a leasehold estate in the land. However, if registration of the lease or instrument of transfer is required under the State or Territory legislation applying when the lessee obtains the leasehold interest, the Commissioner considers that the lease is supplied and acquired when the recipient (or the recipient's agent) obtains:

- unconditional possession of a registrable lease or instrument of transfer of the lease; or
- a lease or an instrument of transfer of lease that would be registrable when it is stamped.

Again, in the case of a sale, this is at settlement.

How is the margin calculated?

48. Unless subsection 75-10(3) or section 75-11 apply, the margin for the supply is calculated under subsection 75-10(2). Under subsection 75-10(2) the margin for the supply is the amount by which the consideration for the supply exceeds the consideration for its acquisition. The consideration for the acquisition is discussed in detail at paragraphs 50 to 69 in GSTR 2005/D4.

[18] Subsections 75-11(1) to (2B) do not apply to real property that you supply, if you acquired it on or before 1 July 2000.

49. If subsection 75-10(3) applies, the margin is the difference between the consideration for the supply and the valuation of the interest, unit or long-term lease at the relevant date. Subsection 75-10(3) applies if an approved valuation has been made and:

(a) the circumstances in section 75-11 do not apply; and

(b) you acquired (or in some cases held) the real property before 1 July 2000; or

(c) you acquired the real property on or after 1 July 2000, but the supply to you:

(i) was GST-free under subsection 38-445(1A); and

(ii) related to a supply before 1 July 2000, by way of lease, that would have been GST-free under section 38-450 had it been made on or after 1 July 2000 (item 2A).

Margin for the supply of real property acquired from a deceased estate

50. Subsections 75-11(3) and (4) address how the margin scheme applies when you supply real property that you acquired by inheriting it. Section 195-1 specifies the manner in which real property can be inherited. It states that you inherit a freehold interest in land, a stratum unit or a long-term lease if you become an owner of the interest, unit or lease:

(a) under the will of a deceased person, or that will as varied by a court order; or

(b) by operation of an intestacy law, or such a law as varied by a court order; or

(c) because it is appropriated to you by the legal personal representative of a deceased person in satisfaction of a pecuniary legacy or some other interest or share in the deceased person's estate; or

(d) under a deed of arrangement if:

(i) you entered into the deed to settle a claim to participate in the distribution of the deceased person's estate; and

(ii) any *consideration given by you for the interest, unit or lease consisted only of the variation or waiver of a claim to one or more other assets that formed part of the estate.

51. Subsection 75-11(3) applies if the deceased acquired the real property before 1 July 2000, while subsection 75-11(4) applies if the deceased acquired the property on or after that date.[19] Both these subsections only apply if subsections 75-11(1) to (2B) do not apply (GST groups and GST joint ventures).

[19] Subsection 75-11(4) is addressed at paragraphs 102 to 105 of GSTR 2005/D4.

52. If you supply real property that you inherit, and the deceased acquired it before 1 July 2000, then paragraph 75-11(3)(ca) allows you to choose to use the consideration for the deceased's acquisition of the real property when calculating the margin for the supply. However, paragraph 75-11(3)(ca) can only apply if:

- you know the amount of the consideration for the deceased's acquisition of the property; and
- you choose to use this amount when calculating the margin for the supply.

53. Under paragraph 75-11(3)(ca) the margin for the supply is the amount by which consideration for the supply you make exceeds the consideration for the deceased's acquisition of the property.

54. If you do not know the consideration for the deceased's acquisition of the real property, or you do not choose to calculate the margin for the supply under paragraph 75-11(3)(ca), then the margin is calculated under paragraph 75-11(3)(d) or 75-11(3)(e).[20]

Paragraph 75-11(3)(d)

55. Paragraph 75-11(3)(d) applies if, immediately before the time that you inherited the real property, the deceased was neither registered or required to be registered. If paragraph 75-11(3)(d) applies, the margin for the supply is the amount by which the consideration for the supply exceeds an approved valuation of the real property as at the latest of:

- 1 July 2000; or
- the day on which you inherited the real property; or
- the first day on which you were registered or required to be registered for GST.

56. It is evident from paragraph 6.29 of the Revised Explanatory Memorandum to the Tax Laws Amendment (2005 Measures No. 2) Bill 2005 that Parliament's intention is that the day on which you inherited the real property will ordinarily be the date of death of the deceased.[21] However, in some circumstances such as where a will is varied by a court order or the beneficiaries of the estate enter into a deed of arrangement, then the day on which you inherited the real property will be the date the court order or deed of arrangement becomes effective.

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[20] Paragraph 75-11(3)(e) does not apply to real property acquired before 1 July 2000. Paragraph 75-11(3)(e) is addressed at paragraph 101 in GSTR 2005/D4.

[21] Paragraph 6-29 of the Revised Explanatory Memorandum to the Tax Laws Amendment (2005 Measures No. 2) Bill 2005 states that 'in most cases the day on which you inherit property is the date of death of the deceased'.

Margin for the supply of real property acquired from an associate

57. Subsection 75-11(7) deals with the supply of real property that you acquired from an associate.[22] It only applies when the other subsections in section 75-11 do not apply.

58. Paragraph 75-11(7)(c) applies if before 1 July 2000 you acquire real property from an entity who was your associate at the time. When you supply the real property, the margin for the supply under paragraph 75-11(7)(c) is the amount by which the consideration for the supply exceeds an approved valuation of the real property as at 1 July 2000.[23]

59. Subsection 75-11(8) extends the application of subsection 75-11(7) to acquisitions through supplies made by the following:

- a GST branch;
- a non-profit sub-entity; and
- a government entity of a kind referred to in sections 72-95 or 72-100,

in the same way as Subdivision 72-D affects the operation of Division 72.

60. The effect of this is that subsection 75-11(7) applies not only to associates as defined in section 195-1 but also treats the following as if they were associates:

(a) a GST branch of an entity as if it were an associate of:

(i) that entity;

(ii) every other GST branch of that entity; and

(iii) any other associate of that entity;

(b) a non-profit sub-entity of an entity as if the non-profit sub-entity were an associate of:

(i) that entity;

(ii) every other non-profit sub-entity of that entity; and

(iii) any other associate of that entity;

(c) a government entity that is:

(i) a Department of State of the Commonwealth;

(ii) a Department of the Parliament;

(iii) an Executive Agency, or Statutory Agency, within the meaning of the *Public Service Act 1999;* or

[22] Under section 195-1, 'associate' is defined as having the meaning given by section 318 of the *Income Tax Assessment Act 1936.*

[23] Paragraph 75-11(7)(d) deals with how the margin scheme applies if you acquire real property on or after 1 July 2000. This is explained at paragraphs 106 to 109 in GSTR 2005/D4.

(iv) an organisation, established by the Commonwealth, of a kind referred to in paragraph (e) of the definition of government entity in section 41 of the *A New Tax System (Australian Business Number) Act 1999,*

as if the government entity were an associate of the Commonwealth, of every other government entity of a kind referred to in paragraph (i), (ii), (iii) or (iv) and of any other associate of the Commonwealth.

Consideration for the supply and settlement adjustments

61. The consideration for the supply and the consideration for the acquisition may be either monetary or non-monetary or both. The consideration for the supply or acquisition will not always be the price shown on the contract as, on settlement, adjustments are commonly made for rates, land tax and other outgoings.

62. Rates or land tax may be assessed to and paid by the supplier before the date of settlement. In such a case, the contract will usually require the recipient to pay an extra amount to the supplier for the balance of the rates or land tax period that reflects the recipient's period of ownership. In the usual case where the contract stipulates that both the purchase price and the adjustment must be paid at settlement, in return for possession and title documents, the supplier is receiving and the recipient is paying extra consideration for the sale and purchase of the land.

63. Alternatively, rates may be assessed to the recipient after settlement even though part of the rates period reflects the supplier's period of ownership prior to settlement. In these circumstances, the terms of the contract usually require an adjustment in favour of the recipient, based on the supplier's and recipient's respective periods of ownership. In that case, the recipient is paying less consideration to the supplier than the purchase price reflected in the contract.

64. In other circumstances, rates or land tax assessed to the supplier as owner of the land in respect of the supplier's period of ownership may remain unpaid at settlement. In this case the recipient may withhold an amount from the purchase price and pay this amount to the municipal or revenue authority. There is no adjustment to the consideration for the land in this case because the purchaser is merely applying part of the agreed consideration to meet the seller's liability for rates or land tax.

Alternative view

65. There is an alternative view that settlement adjustments for rates paid in advance do not change the consideration for the supply of land. On this view, any adjustment made on the transfer of possession in these circumstances is not considered to be in respect of the purchase price of the property, but is a reimbursement of rates for the respective period of usage.

66. Support for this view is found in *Commissioner of Taxation v. Morgan* (1961) 106 CLR 517. The High Court held that a purchaser of income producing property was allowed an income tax deduction for the additional amount paid at settlement for a rates adjustment. In reaching this conclusion, the Court took the view that a settlement adjustment for rates paid in advance is not consideration for the property. Instead, it stated at 106 CLR 521 that:

> [t]he payment of the apportioned part is separate and represents nothing but the reimbursement of a charge for an ensuing period of enjoyment, one of a very limited duration.

67. The Commissioner does not accept that the decision in Morgan's case is applicable in the GST context as the High Court was considering the deductibility of the rates adjustment in a capital versus revenue context under the *Income Tax Assessment Act 1936*. For GST purposes, the relevant factor is the nature of the supply and the nexus, if any, between the payment and that supply. In these circumstances, the Commissioner considers that there is a single supply of real property and the adjustments form part of the calculation of the consideration for the supply. Additionally, the High Court did not have to consider the implications of the definition of consideration under section 9-15 of the GST Act which is broader than the ordinary meaning of that term.

Valuation dates

68. Valuations are required to work out the margin for supplies of real property under paragraph 75-10(3)(b) and in particular circumstances under section 75-11. The table below sets out the valuation dates for the purposes of these provisions.

Section	When valuations may be used	Valuation date
Item 1 of the table in subsection 75-10(3).	You acquired the freehold interest, stratum unit or long-term lease before 1 July 2000 and items 2, 3, and 4 do not apply.	1 July 2000
Item 2 of the table in subsection 75-10(3).	You acquired the freehold interest, stratum unit or long-term lease before 1 July 2000 but you were not registered or required to be registered until after 1 July 2000.	The earlier of the date of effect of your registration or the date on which you applied for registration.

Item 2A of the table in subsection 75-10(3).	You acquired the freehold interest, stratum unit or long-term lease on or after 1 July 2000, but the supply to you: (a) was GST-free under subsection 38-445(1A); and (b) was related to a supply before 1 July 2000, by way of a lease, that would have been GST-free under section 38-450 had it been made on or after 1 July 2000. Note: The terms 'Commonwealth, a State or Territory' and 'improvements' are referred to in subsection 38-445(1A) and section 38-450. The meaning of these terms is discussed at paragraphs 92 to 123.	1 July 2000
Item 3 of the table in subsection 75-10(3).	You are registered or required to be registered and have held the freehold interest, stratum unit or long-term lease since before 1 July 2000, and there were improvements on the land or premises as at 1 July 2000.	1 July 2000
Item 4 of the table in subsection 75-10(3).	The supplier is the Commonwealth, State, or Territory and it has held the freehold interest, stratum unit or long-term lease since before 1 July 2000 and there were no improvements on the land or premises as at 1 July 2000. Note: The terms 'Commonwealth, a State or Territory' and 'improvements' are discussed at paragraphs 92 to 123.	The day on which the taxable supply takes place.
Paragraph 75-11(3)(d).	You inherited the real property and the deceased had acquired the property before 1 July 2000.	The latest of: (a) 1 July 2000; (b) the day that you inherited the real property; or (c) the first day that you registered or were required to be registered.
Paragraph 75-11(7)(c).	You acquired the real property before 1 July 2000 from an associate, and the other subsections in section 75-11 do not apply.	1 July 2000.

Note:

(a) a valuation must be made as at the date specified in column 3 of the table; and

(b) the valuation must comply with all requirements determined in writing by the Commissioner.

Time to make valuations

69. To work out the margin for the supply of real property, you require a valuation as at the valuation date. The valuation process itself does not have to be undertaken on that date.

70. The valuation must be made by the due date for lodgment of the supplier's Activity Statement for the tax period to which the GST on the supply is attributable.

71. However, if the Commissioner has allowed a further period under paragraph 75-5(1A)(b) for the supplier and the recipient to agree in writing that the margin scheme is to apply in working out the GST on the supply, the valuation must be made by the later of:

(i) 6 weeks from the further period that the Commissioner has allowed under paragraph 75-5(1A)(b); or

(ii) 6 weeks from the date of the Commissioner's decision to extend the further period under paragraph 75-5(1A)(b).

72. If the valuation is not undertaken within the time periods specified in paragraphs 70 and 71, the Commissioner may for good reason allow an additional period to obtain a valuation.[24]

What is the real property that you value?

73. If subsection 75-10(3) or any of the provisions of section 75-11 require you to obtain an approved valuation, the real property that you value is the interest, unit or lease that is in existence at the valuation date. This will not always be the real property that is supplied.

74. Often the real property that is supplied was not in existence at the valuation date. Examples of this are:

- land that is acquired as broadacres and is later subdivided and sold; and
- land on which strata units are built.

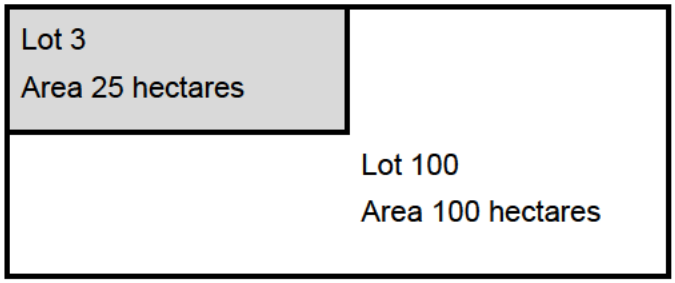
[24] Paragraphs 15 to 17 of *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination MSV 2005/3*. Practice Statement PSLA 2005/16 sets out the circumstances when the Commissioner may exercise the discretion contained in the Determination to extend the period for obtaining a valuation.

75. If the real property that is supplied was not in existence at the valuation date but was, for example, subdivided from the interest that was in existence at that date, the valuation must be made as follows:

(a) a valuation of the interest, unit or lease in existence at the valuation date must be undertaken; and

(b) the valuation of that interest, unit or lease is then apportioned (by the professional valuer if the professional valuation method[25] is used) on any fair and reasonable basis, to ascertain the part of the valuation that relates to the interest, unit or lease that you supplied.

76. This is diagrammatically represented below:



- At 1 July 2000 lot 100 with an area of 100 hectares had a market value of $100,000. After 1 July 2000, lot 100 was subdivided creating lot 3 with an area of 25 hectares.
- The value of lot 3 is the proportion of the valuation of the interest you acquired that is in existence as at 1 July 2000, that is, lot 100. In the context of the diagram above, this proportion is $25,000 (1/4 of $100,000 on the assumption that the land is of approximately uniform value per square metre).

What valuation methods does the Commissioner accept for taxable supplies of real property made on or after 1 December 2005?

77. *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination MSV 2005/3* prescribes the following valuation methods for taxable supplies of real property made on or after 1 December 2005:

(a) a valuation of the market value of the interest, unit or lease at the valuation date determined in writing by a professional valuer provided it is not contrary to professional standards recognised in Australia;[26]

[25] The professional valuation method is discussed at paragraphs 77 to 85.
[26] If subsection 75-10(3A) applies, the determination provides that the valuation must be the market value of the real property determined by a professional valuer as if there are no improvements on the real property on the valuation date. Supplies to which subsection 75-10(3A) applies are addressed in Goods and Services Tax

(b) adopting as the value the consideration in a contract for the sale of real property executed or exchanged before the valuation date by parties dealing at arm's length; and

(c) adopting as the valuation the most recent value as determined before the valuation date by or on behalf of a State or a Territory Government department as the unimproved value, the site value, or the capital value of the land, for rating or land tax purposes.

78. Under subsection 75-35(2), a valuation made in accordance with the requirements in the determination is an approved valuation.

Method 1: Valuation of the market value determined by a professional valuer

79. Under Method 1, the valuation is the market value of the interest, unit or lease that you held at the valuation date (or if item 2A applies, the interest you later acquired) determined in writing by a professional valuer, provided it is not contrary to professional standards recognised in Australia.

80. The exception to the above is when item 4 in the table in paragraph 75-10(3)(b) applies and there are improvements on the land when the taxable supply is made. In these circumstances, the valuation is to be made as if there were no improvements on the land or premises at 1 July 2000.[27]

81. Item 4 applies if:

- the supply is made by the Commonwealth, a State or a Territory;
- the Commonwealth, a State or a Territory held the interest, unit or lease since before 1 July 2000; and
- at 1 July 2000 there were no improvements on the land or premises in question.

Professional valuers

82. A professional valuer[28] is:

(a) a person registered or licensed to carry out real property valuations under a Commonwealth, State or Territory law;

(b) a person who carries on business as a valuer in a State or Territory where that person is not required to be licensed or registered to carry on a business as a valuer; or

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Rulings GSTR 2000/21 and GSTR 2005/D5. GSTR 2005/D5 also discusses the meaning of the terms relevant to subsection 75-10(3A).

[27] Subsection 75-10(3A).

[28] Refer to the definition section of the Determination in Schedule 1.

(c) a member of the Australian Property Institute who is accredited as a Certified Practising Valuer.

83. You may use an in-house employee who is a professional valuer.

84. A supplier may engage a professional valuer to undertake the valuation or accept a valuation made by a professional valuer commissioned by another party, for example, a purchaser.

Documentation that a professional valuer is required to provide

85. The valuation must include a signed certificate which specifies:

(a) a full description of the property being valued;

(b) the applicable valuation date (refer to the table in paragraph 68);

(c) the date the valuer provides the valuation to the supplier;

(d) the market value of the property at the valuation date;

(e) the valuation approach and the valuation calculation; and

(f) the qualifications of the valuer.

Method 2: A valuation by adopting the consideration provided by a purchaser in a contract for the sale and purchase of real property

86. A valuation can be made by adopting as the valuation the consideration provided by a purchaser in a contract for the sale and purchase of real property executed or exchanged before the valuation date between parties dealing at arm's length.[29]

Method 3: Valuation by adopting value as determined by a State government or a Territory government

87. A valuation can be made by adopting as the value the most recent unimproved value, site value, or the capital value of the land as determined by a valuation by a State or a Territory Government, or by a professional valuer on behalf of a State or a Territory Government, for rating or taxing purposes made before the valuation date.

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[29] Judicial interpretation of the phrase 'dealing at arm's length' can be found in *Collis v. FC of T* (1996) 33 ATR 438; 96 ATC 4831, *Granby v. FC of T* (1995) 30 ATR 400; 95 ATC 4240; (1995) 129 ALR 503, *Barnsdall v. FC of T* (1988) 19 ATR 1352; 88 ATC 4565, *The Trustee of the Estate of the Late AW Furse No. 5 Will Trust* (1990) 21 ATR 1123; 91 ATC 4007.

88. The amount that may be adopted as the valuation as at the valuation date is the value shown in a notice of valuation or land tax notice of assessment or other similar document.

How to use the professional valuer's method when you have previously used the cost of completion method

89. For supplies made on or after 1 July 2005, you cannot use the cost of completion method to value the interest that you held at the valuation date, except in the limited circumstances covered by *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination MSV 2005/2*.[30] Instead, a valuation must be made using either method 1, 2 or 3.

90. If you use the professional valuer's method for taxable supplies made on or after 1 December 2005 and:

(a) before 1 December 2005 you commenced a development on land that you held at the valuation date;

(b) you had made taxable supplies of real property subdivided from this land before 1 December 2005 and had used the cost of completion valuation method for all of these supplies; and

(c) you make taxable supplies of real property subdivided from this land on or after 1 December 2005,

then a valuation of the entire interest you held at the valuation date must be made in accordance with one of the approved methods. The part of the valuation amount that relates to the supplies that you make on or after 1 December 2005 must be ascertained using any fair and reasonable basis of apportionment.

Example 1: using the professional valuer's method when cost of completion method previously used

91. *James is a property developer who has been registered for GST since 1 July 2000. At 1 July 2000 he held a large tract of broadacre land, which he intended to sell as part of a multi-staged development. At 30 June 2005 he had sold four of the five stages of the development under the margin scheme, and had used the cost of completion method to value the land and used that value to work out the margin for these supplies. The fifth stage of the development will be sold on or after 1 July 2005. To calculate the margin for the supplies for the fifth stage of the development, the value of the entire tract of broadacre land held at 1 July 2000 (the valuation date) must first be ascertained. Then the part of the valuation that relates to the*

[30] *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination MSV 2005/2* extends the operation of the costs of completion valuation method to supplies made after 1 July 2005, where the contract for the supply was entered into before that date.

fifth stage of the development must be determined using any fair and reasonable basis.

Commonwealth, a State or a Territory

92. Whether a supply is made by the Commonwealth, a State or a Territory is relevant for establishing which item in the table contained in subsection 75-10(3) applies to the supply.

93. If the Commonwealth, State or Territory supplies land on which there are no improvements the supply is GST-free under subsection 38-445(1), provided the land has not been previously supplied as a GST-free supply under this section.

94. If the land was held before 1 July 2000 and there were improvements on the land as at 1 July 2000, then the Commonwealth, a State or a Territory can choose the margin scheme to calculate the GST payable on the supply under item 3 in the table in subsection 75-10(3). However, if the land has no improvements as at 1 July 2000 but there are improvements subsequently made to the land before it is supplied, the Commonwealth, a State or a Territory can work out the GST, on the difference between the consideration for the supply and the valuation of the land at the date of supply, as if there were no improvements on the land at the date of supply.[31]

95. The Commissioner considers that for the purposes of items 2A and 4 the Commonwealth, a State or a Territory includes a department, agency or organisation of the type referred to in the definition of 'government entity' in section 195-1. This means that the Commonwealth, a State or a Territory, as the case may be, includes any of the following:

(a) a Department of State of the Commonwealth;

(b) a Department of the Parliament;

(c) an Executive Agency, or Statutory Agency, within the meaning of the *Public Service Act 1999*;

(d) a Department of State of a State or Territory;

(e) an organisation that:

  (i) is not an entity;[32] and

  (ii) is either established by the Commonwealth, a State or a Territory (whether under a law or not) to carry on an enterprise or established for a public purpose by an Australian law; and

[31] Subsection 75-10(3A).

[32] Entity is defined for this purpose in section 37 of the *A New Tax System (Australian Business Number) Act 1999* in the same terms as the definition of 'entity' in section 184-1 of the GST Act.

(iii) can be separately identified by reference to the nature of the activities carried on through the organisation or the location of the organisation;

whether or not the organisation is part of a Department or branch described in paragraph (a), (b), (c) or (d) or of another organisation of the kind described in this paragraph.[33]

96. The Commonwealth, a State or a Territory is not limited to these departments, agencies and organisations and may include a corporation which is a 'government entity' as defined in section 195-1. However, not every corporation in which the Commonwealth or a State or Territory has an interest is part of the Commonwealth or the State or Territory.

97. The Commissioner considers that this issue is to be determined in accordance with the principles developed by the High Court of Australia in the cases concerning the meaning of 'a State' in section 114 of the Australian Constitution, most recently in *SGH Ltd v. Commissioner of Taxation* [2002] HCA 18 (the *SGH* case).[34] The discussion which follows is drawn from these cases. For ease of reference, the discussions refer to a State, as that is the context in which the issue most commonly arises for GST purposes, but the principles apply equally in determining whether a corporation is the Commonwealth or a Territory. Similarly, while the discussion focuses upon corporations, many of the principles could apply to other structures, such as a trust.

98. The fundamental principle established by these cases is that, if the corporation is discharging governmental functions for the State – that is, the State is carrying on the relevant business or other function through the corporation – the corporation is the State.[35] On the other hand, if the intention is for the corporation to perform its functions independently of, and not as an instrument of, the State – so that the concept of a State activity cannot be realistically applied to that which the corporation does – the corporation is not the State.[36]

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[33] Under section 195-1, 'government entity' has the meaning given by section 41 of the *A New Tax System (Australian Business Number) Act 1999*.

[34] Other relevant cases include *South Australia v. The Commonwealth of Australia & Anor* [1992] HCA 7; 1993 174 CLR 235 ('*South Australia v. The Commonwealth*'), *Deputy Commissioner of Taxation v. State Bank of New South Wales* (1992) 174 CLR 219 ('*DCT v. State Bank* '), *State Bank of NSW v. Commonwealth Savings Bank of Australia* (1986) 161 CLR 639 ('*State Bank NSW v. Commonwealth Savings Bank*'), *Superannuation Fund Investment Trust v. Commissioner of Stamps* (SA) (1979) 145 CLR 330 ('the *SFIT* case'), and *Inglis v. Commonwealth Trading Bank of Australia* (1969) 119 CLR 334 ('*Inglis*').

[35] See the joint judgment in the *SGH* case at paragraph 16. The issue is not determined by asking whether the entity is entitled to the privileges and immunities of the Crown: *SGH case* at paragraph 15.

[36] See *Inglis*, per Kitto J at paragraph 4, adopted by the joint judgment in *State Bank NSW v. Commonwealth Savings Bank* at paragraph 3.

99. To determine which of these characterisations applies in a particular case, the following principles should be considered:

(a) whether a corporation is the State requires consideration of every feature relevant to its relationship with the State;[37]

(b) it is the ownership and management of a corporation, and the purposes it is required to pursue, that will most often reveal whether the corporation is the State. If examination of those features reveals that the corporation is wholly owned and controlled by the State, and must act solely in the interests of the State, the conclusion that it is the State will readily follow;[38]

(c) it follows that it is not sufficient to demonstrate a government policy of favouring or facilitating the creation of the corporation in pursuit of some aspect of the public interest. If the State does not control the conduct of the affairs of the corporation, the State cannot be said to be carrying on activities of government through the corporation.[39] It is for this reason that local governments are not regarded as part of the State;[40]

(d) a provision that the corporation must pursue the interests of the State or the public or that its policies could be determined by the executive government of the State is an indicator that the corporation is the State; [41]

(e) conversely, a provision that positively permits the corporation to take account of other external interests is a contrary indicator.[42] An example would be such a provision in relation to the interests of shareholders who do not represent the State;

(f) a corporation may be the State even though its functions are not traditional and inalienable functions of government, but extend to commercial functions.[43] However, that a corporation's functions are traditional or generally accepted governmental functions may assist in forming the view that the corporation is an instrument of the State;[44]

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[37] See the joint judgment in the *SGH* case at paragraph 22.
[38] See the joint judgment in the *SGH* case at paragraph 22.
[39] See the joint judgment in the *SGH* case at paragraph 22.
[40] *Sydney City Council v. Reid* 34 NSWLR 506 per Kirby P (as he then was).
[41] See the joint judgment in the *SGH* case at paragraph 31 and Callinan J at paragraph 131. Also, *Inglis* per Kitto J (with whom Windeyer J agreed) at paragraph 8.
[42] See the joint judgment in the *SGH* case at paragraphs 28 and 32.
[43] *DCT v. State Bank* at paragraph 21.
[44] *Inglis* per Kitto J (with whom Windeyer J agreed) at paragraph 4.

(g) the participation of the executive government in formulating policy and making decisions is an indicator that the corporation is the State.[45] For example, a power for a Minister or the Executive Council to override decisions of the board is indicative that the corporation is an instrument of the State;

(h) conversely, the absence of control by the executive, and the absence of guidelines in the exercise of its functions, point to the corporation not being the State.[46] However, the weight to be given the absence of a power to interfere with the day to day control of the corporation's activities will depend upon the occasion for the exercise of such a power. The absence of the power will be of little significance where the occasion for the exercise of it would be rare, such as where a duty to pursue the interests of the State or the public is imposed on the Board in any case;[47]

(i) the absence of corporators (shareholders) has been held to be a relevant factor indicating that the corporation may be the State;[48]

(j) the ability of the executive government to control the appointment and, more particularly, the removal of directors is consistent with a conclusion that the corporation is the State;[49]

(k) the financial arrangements for the corporation are likely to be indicative. These include whether there is a requirement that the corporation's accounts are to be audited by the State Auditor-General and the results reported to the State's Treasurer, whether the corporation's borrowings are guaranteed by the State or may only be made with the consent of the Treasurer, and the destination of profits of the corporation, that is, whether they are distributed to the State;[50]

(l) a regulatory role, even a modest one, such as the power to make by-laws, is an indicator that the corporation is an instrument of the State;[51]

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[45] See the joint judgment in the *SGH* case at paragraph 22 and Callinan J at paragraph 131.
[46] See generally the *SFIT* case.
[47] *State Bank of NSW v. Commonwealth Savings Bank* at paragraph 16.
[48] See the *SGH* case per Callinan J at paragraph 131; *State Bank of NSW v. Commonwealth Savings Bank* at paragraphs 3 and 11; *Inglis* per Kitto J (with whom Windeyer J agreed) at paragraphs 6.
[49] See the *SGH* case per Callinan J at paragraph 131; *State Bank of NSW v. Commonwealth Savings Bank* at paragraph 12; *Inglis* per Kitto J (with whom Windeyer J agreed) at paragraph 10.
[50] *State Bank of NSW v. Commonwealth Savings Bank* at paragraph 14.
[51] *State Bank of NSW v. Commonwealth Savings Bank* at paragraph 14.

(m) in the consideration of whether a corporation is the Commonwealth, a requirement for the corporation to pay income tax is unlikely to be relevant. It may increase the Commonwealth's participation in profits of the corporation, but otherwise it merely assimilates the financial accounts of the corporation or those of other non-government corporations.[52] The Commissioner considers that similar comments apply in respect of an obligation to pay income tax equivalents under National Compensation Policy arrangements; and

(n) while it may be that there is no impediment to a corporation established under the general corporations or associations incorporation law being the State, the Commissioner is not aware of any decided case where such a corporation has been held to be the State.[53] A submission that such a corporation is the State would require careful consideration by the Tax Office. This is so whether the corporation's shares are owned directly by the State, such as through a Minister of the Crown, or by another corporation controlled by the State.

Supplies between Commonwealth, State or Territory entities

100. A supply between two Commonwealth, State or Territory departments or other government entities is a taxable supply if the requirements in section 9-5 are satisfied. That is so even if the supplier and recipient entities are each part of the Commonwealth or the same State or Territory.

Example 2: taxable supply between two government entities

101. *Prior to 1 July 2000, government Department A in Victoria acquired land on which there where no improvements. The Department constructed an office building on the land and then sold the land to government entity B which is also part of the State of Victoria. If the sale satisfies the requirements of section 9-5 it is a taxable supply.*

[52] *Inglis* per Kitto J (with whom Windeyer J agreed) at paragraph 10.

[53] See Gummow J in the *SGH* case at paragraph 63 where it is suggested that drawing a distinction between a 'general' and a special or particular law of corporations in the context of section 114 of the Constitution would be to complicate the section, 'which is concerned with matters of substance rather than form'. On the other hand, Callinan J at paragraph 149 thought it 'not irrelevant' that SGH was not created directly by the State but by another corporation which was the State. Contrast *The Commonwealth of Australia v. Bogle* (1953) 89 CLR 229 per Fullagar J (with whom Dixon CJ and Web and Kitto JJ agreed) at 267-268.

102. *If the supplier, Department A, calculates the GST on this supply under the margin scheme, the effect of subsection 75-10(3A) is that, for the margin to be calculated under subsection 75-10(3), the valuation must be undertaken as if there were no improvements on the land or premises at the valuation date.*

103. In some circumstances, for example as part of a transfer of departmental responsibilities, real property that was acquired by one government department or agency is vested by an Act of Parliament in another government department or agency. Both government departments or agencies are part of the Commonwealth or the same State or Territory as the case may be. Where the real property was acquired by the first entity before 1 July 2000 and vested in the other government entity on or after this date, item 4 of the table in subsection 75-10(3) may apply to a subsequent supply by the second entity if there were no improvements on the land or premises as at 1 July 2000. This is because, although the land is vested in the second entity on or after 1 July 2000, both entities are part of the Commonwealth or the same State or Territory, as the case may be, which has held the interest since before 1 July 2000.

104. However, while the two government entities are registered for GST purposes, subsection 149-5(2) and section 149-15 treat each entity, although part of the Commonwealth or the same State or Territory, as if it were a separate entity. Accordingly, if the first entity made a taxable supply by way of sale to the second entity, GST would be payable. Further, if the first entity did not apply the margin scheme in working out the GST on the supply, the second entity would not be able to apply the margin scheme to a subsequent supply of the land: subsection 75-5(2). In other words, while it is accepted that the Commonwealth or the same State or Territory held the land at 1 July 2000 and subsequently sold the land, the entities are nevertheless treated as separate entities for GST purposes as required by Division 149.

'Land on which there are no improvements' and 'no improvements on the land'

When do you ascertain whether there are no improvements on the land

105. The terms 'land on which there are no improvements' and 'no improvements on the land' are relevant to the application of items 2A and 4 in the table in subsection 75-10(3).

106. For item 2A, the relevant day for ascertaining whether there were no improvements on the land is *when it was previously supplied* by the Commonwealth, a State or a Territory under a lease that was GST-free under subsection 38-450(1). For item 4, there must have been no improvements on the land or premises at 1 July 2000.

107. In some circumstances, improvements may have been on the land but no longer exist as improvements on the relevant day specified in the table. For example, bushland owned by the Commonwealth, a State or a Territory may have originally been fenced, but due to deterioration no valuable fencing remains at 1 July 2000.

108. While when it was first erected the fencing was an improvement to the land, as no valuable fencing remains as at 1 July 2000, for the purposes of item 4 in the table there would have been no improvements on the land at the relevant date in this case.

The meaning of 'land on which there are no improvements' and 'no improvements on the land'

109. There have been numerous cases, several at the High Court of Australia, addressing the meaning of 'improvements thereon or appertaining to' or similar expressions in the context of land tax and rating statutes.[54] Each has taken a broad view of the meaning of the expression, that is, not limiting it to visible structural improvements but taking it to embrace clearing, draining and any other operation on the land that has the effect of enhancing its value.

110. Applying this principle when interpreting the words 'land on which there are no improvements' and 'no improvements on the land' means that the term 'improvements' refers to any improvements through human intervention 'on' the land which have the effect of enhancing its value.

111. Where the following examples enhance the value of the land, they are 'improvements on the land' for the purposes of the subsection 75-10(3A) and the table in paragraph 75-10(3)(b):[55]

- houses, town-houses, stratum units, separate garages, sheds and other out-buildings;
- commercial and industrial premises;
- farm houses, farm outbuildings, internal fencing, stockyards, wells and bores, excavated tanks, dams, surface drains, culverts, bridges, sown pasture, formed internal roads, and irrigation layouts;

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[54] The most commonly cited case seems to be *Morrison and others v. Federal Commissioner of Land Tax* (1914) 17 CLR 498. For a more detailed discussion, see *McGeogh v. Federal Commissioner of Land Tax* (1929) 43 CLR 277. Also, *Fisher v. Deputy Federal Commissioner for NSW Land Tax* (1915) 20 CLR 242; and *Keogh v. Deputy Federal Commissioner of Land Tax for NSW* (1915) 20 CLR 258. See also *Ex parte George Thomas* (1881) 2 LR NSW 39, a case concerning compensation for improvements 'upon' the land, an expression that Manning J at 44 took to mean no more than that 'the improvement should not be out of the land', such that ringbarking was an improvement, Martin CJ and Windeyer J reaching the same conclusion.

[55] The discussion on improvements is applicable to subsection 38-445(1A) and section 38-450. Both these provisions are referred to in item 2A in the table in paragraph 75-10(3)(b).

- formed driveways, swimming pools, tennis courts, and walls;
- any other similar buildings or structures;
- fencing – internal or boundary fencing;
- clearing of timber, scrub or other vegetation;
- excavation, grading or levelling of land;
- drainage of land;
- building up of soil fertility;
- removal of animal pests, rabbit burrows etc.;
- removal of rocks, stones or soil; and
- filling of land.

112. The fact that a particular human intervention results in a decrease in the value of land does not necessarily mean that there are no other improvements on the land.[56] In limited circumstances, a building may be a detriment. For example, a building that is uninhabitable because it is derelict, is not capable of being repaired and does not enhance the value of the land is a detriment rather than an improvement. However, usually there will be other improvements on the land, in particular, clearing. In those circumstances, there are improvements on the land notwithstanding the presence of the derelict building.

113. In some circumstances, human intervention on land results in neither an improvement nor a detriment, as it neither enhances nor decreases the value of land. Examples of this are as follows:

- fire breaks, where their purpose is solely to allow access to fire equipment and reduce the spread of a fire and which do not enhance the value of the particular land; and
- a fence that is in such disrepair that it does not enhance the value of the land, but is capable of being easily removed.

Improvements that are not on the land

114. The value of land may be enhanced by amenities, such as public roads or railways, or increased settlement in the neighbourhood. While these factors may enhance the value of the land they are not improvements on the land for item 2A and item 4 purposes.

[56] *Brisbane City Council v. Valuer-General (Queensland)* (1978) 140 CLR 41 at 51 discusses a circumstance where human intervention is not an improvement.

Summary

115. In summary, to ascertain whether there are improvements on the land the following factors are taken into account:

- whether the alteration to the land enhances the value of the land;
- whether the improvement exists at the relevant date in the table in subsection 75-10(3); and
- whether the improvement is on the land.

Alternative view

116. There is an alternative view that the expression 'improvements on the land' is limited to visible structural improvements such as buildings and does not extend to things such as clearing and draining.

117. This view does not accept that the principles in the cases referred to at paragraph 109 apply when considering whether there are 'improvements on the land', as these cases considered a broader expression, being 'improvements thereon or appertaining to' the land. The expression is broader, on this view, because the words 'appertaining to the land' extend the phrase to improvements that are not necessarily on the land.

118. However, in *Brisbane City Council v. Valuer-General (Queensland)* [1978] HCA 40, Gibbs J, with whom the four other members of the Court agreed, when considering the meaning of the phrase 'thereon or appertaining thereto', noted at 47 that:

> [t]his means that the improvements, if not on the land, must be 'such as are in the strict legal sense 'appurtenant' to the property and incident to its ownership' (*McDonald v. Deputy Federal Commissioner of Land Tax (NSW)* (1915) 20 CLR 231, at pp 234-235).

119. From the above it can be seen that the words 'appertaining to' only extend the meaning of the phrase to a limited extent. Given this, it seems that the conclusions in the rating and land tax cases are more likely based on the expression 'improvements thereon' rather than the improvements 'appertaining to' the land.

120. As the phrase 'improvements thereon' is analogous to 'improvements on the land', it is the Commissioner's view that the principles in the rating and land tax cases apply when ascertaining the meaning of 'improvements on the land'.

121. The alternative view also argues that the construction adopted in the rating and land tax cases may have been influenced by the perceived policy of that legislation, and consequently the decisions do not have application in the GST context.

122. In *McGeogh v. Federal Commissioner of Land Tax* (1929) 43 CLR 277, per Knox CJ and Dixon J at 290, the policy intent of the relevant legislation was articulated in the decision, in which the purpose of land tax was described as a policy of taxing the 'unearned increment'. That is, without regard to improvements effected by the owner or the owner's predecessors, but having regard to extrinsic circumstances, such as public roads or railways, increased settlement in the neighbourhood and other benefits not brought about by the operations on the land of successive operators. However, this reference to the apparent policy of land tax was not the primary basis for the decision.

123. For the above reasons, on balance, the Commissioner considers the better view to be that improvements on the land, in the GST context, are not limited to visible structural improvements. This view is consistent with the Explanatory Memorandum which refers to the provisions requiring that the land is 'unimproved' or land that 'has not been improved'.[57]

Can you apply the margin scheme when you make a supply of real property and the supply is partly taxable and partly input taxed or partly taxable and partly GST-free?

124. If a supply of real property is partly input taxed and partly taxable or partly taxable and partly GST-free (a mixed supply), then the margin scheme can apply to the taxable component. Examples of supplies that may be such mixed supplies are:

- a supply of a building that contains areas that are residential premises (the supply of which is input taxed) and commercial premises (the supply of which is a taxable supply); or
- a supply of a building that includes new residential premises (the supply of which is a taxable supply) as well as an area supplied as a GST-free supply of a going concern.

125. In these circumstances, if the margin for the supply is calculated under subsection 75-10(2), the consideration for the supply and the consideration for the acquisition, are the amounts of the consideration that relate to the taxable component of the supply.

126. If the margin for the supply is calculated using an approved valuation then the consideration for the supply and the approved valuation are the amounts that relate to the taxable component of the supply.

[57] Explanatory Memorandum to the A New Tax System (Goods and Services Tax) Bill 1998, paragraph 5.132.

Approved valuation

127. The table in paragraph 68 specifies when an approved valuation is required to work out the margin for the supply.

128. If an approved valuation is required to work out the margin for the taxable component of a supply, the valuation is to be obtained for the entire real property supplied. The valuation is then apportioned on any fair and reasonable basis to ascertain the part of the valuation that relates to the taxable component of the supply.

Increasing adjustments for supplies made on or after 17 March 2005, where part of the acquisition was ineligible for the margin scheme

Subsection 75-22(1)

129. You may use the margin scheme if part of your acquisition was ineligible for the margin scheme.[58] An example of this is where a supplier acquires two adjoining properties and one of the properties was acquired as a taxable supply without using the margin scheme, and the other property was acquired as:

- a taxable supply using the margin scheme; or
- an input taxed, GST-free or non taxable supply.[59]

130. If you apply the margin scheme in these circumstances, you have an increasing adjustment to the extent of any input tax credit entitlement that arose for the acquisition through the taxable supply.

131. Subsection 75-22(1) applies to supplies made on or after 17 March 2005 and may apply to:

(a) the subdivision of broadacres; or

(b) construction of stratum units.

Subdivision of broadacres

132. If you acquire adjoining properties, one of which is acquired through a supply that is ineligible for the margin scheme, and you subdivide the properties, the margin scheme can be used for the supply of some of the lots created from the subdivision.

---

[58] Subsection 75-5(2) precludes a supply from being made under the margin scheme if you acquired the entire freehold interest, stratum unit or a long term lease through a supply that was ineligible for the margin scheme. Subsection 75-5(3) sets out the circumstances in which a supply of real property is ineligible for the margin scheme. Paragraphs 31 to 34 of GSTR 2005/D4 contains a discussion on supplies that are ineligible for the margin scheme.

[59] A non taxable supply is a supply that is not taxable, GST-free or input taxed. A common example is a supply by an entity that is not registered or required to be registered for GST.

133. The margin scheme:

- cannot be applied for the supply of those lots that were derived *entirely* from land that was acquired through a supply that was ineligible for the margin scheme as subsection 75-5(2) applies;
- can be applied to those lots derived partly from land that was acquired through a supply that was ineligible for the margin scheme as subsection 75-5(2) does not apply. However, you have an increasing adjustment to the extent of the input tax credit entitlement for the acquisition of the land from which these lots were created; and
- can be applied for the supply of those lots that were derived *entirely* from land that was acquired through a supply that was eligible for the margin scheme.

134. This is diagrammatically represented below as:

4.5 hectares acquired by taxable supply without the margin scheme being applied	4.5 hectares acquired before 1 July 2000

- The land is then subdivided into 9 one hectare blocks.

1	4		7
2	5		8
3	6		9
↑	↑		↑
Ineligible for margin scheme.	Margin scheme applies but there is an increasing adjustment to extent of input tax credits claimed.		Margin scheme applies.

135. In the context of the diagram, the real property that was acquired through a supply that would have been ineligible for the margin scheme is shaded.

136. The margin scheme cannot apply to the supply of Lots 1 to 3 as they were acquired *entirely* through a supply that was ineligible for the margin scheme under subsection 75-5(2). The margin scheme can apply to the supply of lots 7 to 9 because subsection 75-5(2) does not apply to make the supply of them ineligible. The margin scheme can also apply to the supply of lots 4 to 6 as the entire interest in each of those lots was not acquired through a supply that was ineligible for the margin scheme. They are therefore not excluded by subsection 75-5(2).

137. If the margin scheme is applied to the supply of lots 4 to 6, there is an increasing adjustment under subsection 75-22(1). The increasing adjustment for each supply is the relevant proportion of the input tax credit for the acquisition of the land. You may use any fair and reasonable basis of apportionment in working out the extent of the increasing adjustment.

Stratum unit

138. 'Stratum unit' is defined in section 195-1 as having the meaning given by subsection 124-190(3) of the *Income Tax Assessment Act 1997*. Subsection 124-190(3) defines a stratum unit as 'a lot or unit (however described in an Australian law or a foreign law relating to strata title or similar title) and any accompanying common property.' The Commissioner considers that the reference to 'similar title' in the definition of stratum unit includes other arrangements such as group title arrangements.

139. The definition of stratum unit in section 195-1 encompasses a legal arrangement where real property is divided into units or allotments and common property. The common property is usually held by a body corporate as agent for the land owners as tenants in common.

140. For the purpose of the discussion below, the term 'strata title' refers to a strata plan where the boundaries of unit are defined by reference to the structures (for example, walls floors and ceilings). For example, a single building divided into units.

141. In the discussion below the term 'group title' refers to arrangements where the real property is divided into allotments of land and common property. The boundaries are defined by reference to land rather than by reference to building structure.

Strata title

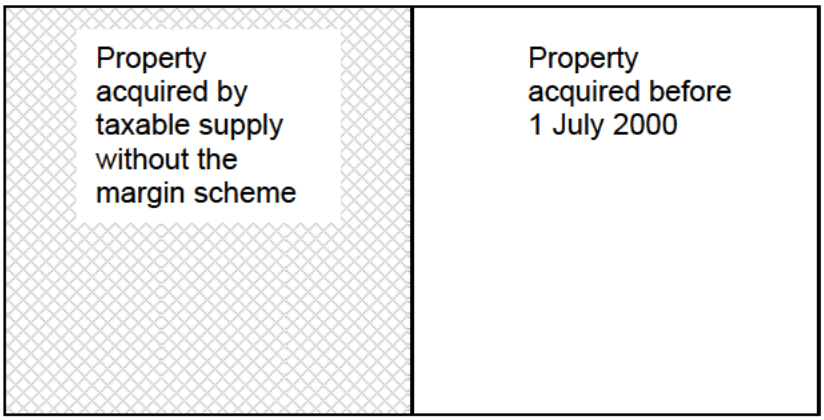
142. If you acquire adjoining properties, one of which was acquired through a supply that is ineligible for the margin scheme, and you then construct stratum units on the properties, then ordinarily some part of the common property will be constructed on land that was acquired through:

- a supply that is eligible for the margin scheme; and

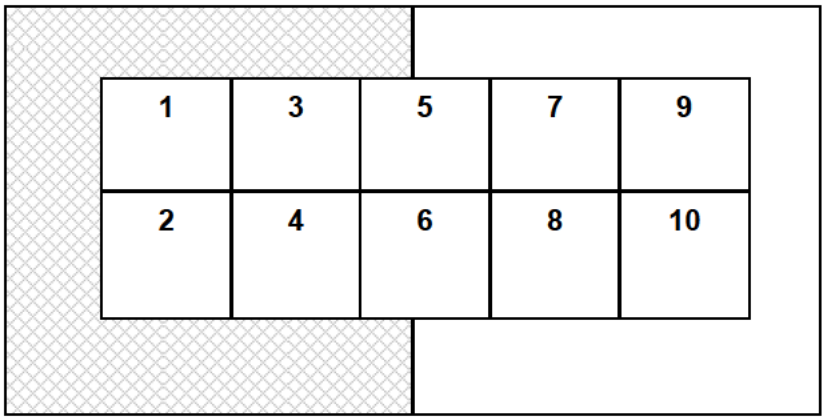
- a supply that is ineligible for the margin scheme.

143. In these circumstances, all of the stratum units have been partly derived from land that was acquired through a supply that was ineligible for the margin scheme. The supply of these units can be made under the margin scheme as subsection 75-5(2) does not apply. However, because the units were partly acquired through land that was acquired through a supply that was ineligible for the margin scheme you have an increasing adjustment under subsection 75-22(1). The increasing adjustment is the proportionate amount of the input tax credits for the acquisition of the land referable to the supply of each stratum unit.

144. This is diagrammatically represented below as:



- 10 stratum units are then built on the land.



145. The real property that was acquired through a supply that would have been ineligible for the margin scheme is shaded in the diagram.

146. The common property in this example is made up of property that was acquired through a supply that would have been ineligible for the margin scheme as well as property that was eligible for the margin scheme.

147. Therefore, the margin scheme can apply to the supply of all the stratum units as the entire interest in each of the stratum units, including the common property, was not acquired through a supply that was ineligible for the margin scheme. They are therefore not excluded from the margin scheme by subsection 75-5(2).

148. If the margin scheme is applied to the supply of any of the stratum units, there is an increasing adjustment under subsection 75-22(1). The increasing adjustment is equal to the proportion of the input tax credit for the acquisition of the land that relates to the stratum unit supplied. To ascertain the extent of the increasing adjustment, you may use any reasonable basis of apportionment.

Group title

149. The margin scheme can be used in group title arrangements where:

- the allotment and the common property have been entirely derived from land that was acquired through a supply that was eligible for the margin scheme;
- the allotment was derived entirely from land that the margin can apply to but some or all of the common property was derived from land that was acquired through a supply that was ineligible for the margin scheme. In these circumstances, you have an increasing adjustment to the extent of the input tax credit entitlement in respect of the acquisition of the lot; and
- both the allotment and the common property were partly derived from land that was acquired through a supply that was ineligible for the margin scheme. However, in these circumstances, you have an increasing adjustment to the extent of the input tax credit entitlement in respect of the acquisition of the lot.

Subsection 75-22(2)

150. Subsection 75-22(2) applies to supplies made on or after 17 March 2005. Under subsection 75-22(2), you may use the margin scheme if you inherit real property and the deceased acquired part of that property through a supply that was ineligible for the margin scheme. An example of this is where:

- you inherit real property from the deceased;

- the deceased acquired two adjoining properties – one of the properties acquired was acquired through a supply that was ineligible for the margin scheme and the other property was acquired through a supply to which was eligible for the margin scheme; and
- the deceased subdivided the properties, or constructed stratum units on them.

151. If you apply the margin scheme in these circumstances you have an increasing adjustment to the extent of any input tax credits for the acquisition of the land.

152. The increasing adjustment is worked out in the same manner as indicated in paragraphs 137 and 143.

Supplies made on or after 17 March 2005 where the full consideration for the acquisition has not been paid

153. If an entity makes a supply of real property but does not pay the full contract price for the acquisition of that property, section 75-12 applies. It provides that the margin for the supply is worked out as the amount by which the consideration for the supply exceeds the consideration *paid* for the acquisition (which may not be the consideration for the acquisition reflected in the contract). Section 75-12 applies to supplies made on or after 17 March 2005.

Example 3: full consideration not paid

154. *Terry supplies real property to Adam. The consideration for the supply is $770,000. However, Adam only pays Terry $700,000. Adam then sells the property to Wendy for $1,100,000 and uses the margin scheme to calculate the GST payable on the supply. When Adam calculates the margin for the supply, the consideration for the acquisition is the amount he paid Terry ($700,000).*

155. *The margin for the supply is $400,000 ($1,100,000 - $700,000).*

Decreasing adjustment for later payment of consideration

156. If section 75-12 applies, and you later make a further payment of the acquisition consideration, you have a decreasing adjustment under section 75-27. Subsection 75-27(2) applies to supplies made on or after 17 March 2005. It provides that the amount of the decreasing adjustment is equal to 1/11th of the further amount of consideration paid.

Example 4: consideration later paid

157. *Using the facts in the example shown above, if Adam subsequently pays Terry the remaining $70,000, Adam has a decreasing adjustment of $6,364 (1/11 × $70,000).*

Entitlement to input tax credits

158. If the GST payable on a supply of real property has been worked out under the margin scheme, the acquisition of the property by the recipient of the supply is not a creditable acquisition. This means that the recipient is not entitled to an input tax credit for the acquisition of the real property.[60]

Tax invoices

159. A supplier is not required to issue a tax invoice for a taxable supply that is solely a supply of real property under the margin scheme.[61]

Record keeping requirements

160. Section 70 of the *Tax Administration Act 1953* requires you to keep records that record and explain all transactions and other acts that you engage in that are relevant to the supply. You must retain these records for at least 5 years after the completion of the transactions or acts to which they relate.

161. As well as retaining accounting records documenting the transaction, you must also retain records showing how you have applied the margin scheme. Examples of these records include:

(a) contracts of sale and purchase;

(b) details of how you worked out the margin for any supply of real property under the margin scheme; and

(c) documents describing the real property at the date it was acquired.

162. For supplies made on or after 17 March 2005, the following records must also be retained, if applicable:

(a) the approved valuation you obtained;

(b) any written request for a further period to obtain an approved valuation and the Tax Office response; and

(c) if an approved valuation is required, documents describing the real property at the valuation date.

163. For supplies made on or after 29 June 2005[62] to which subsection 75-5(1A) applies, the following records must also be retained, if applicable:

(a) the agreement in writing to use the margin scheme; and

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[60] Section 75-20.
[61] Section 75-30.
[62] The date of Royal Assent of the 2005 Amendment Act.

(b) the request for a further period in which to agree to use the margin scheme and the Tax Office response.

Your comments

164. We invite you to comment on this draft Goods and Services Tax Ruling. Please forward your comments to the contact officer(s) by the due date.

Due date:	**11 November 2005**
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Detailed contents list

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Commissioner of Taxation
4 October 2005

Previous drafts:

Not previously issued as a draft

Related Rulings/Determinations:

GSTR 1999/1; GSTR 2000/21; GSTR 2005/D4; GSTR 2005/D5

Subject References:

- freehold interest
- long-term lease
- margin
- margin scheme
- real property
- stratum unit
- taxable supply
- valuation

Legislative References:

- ANTS(ABN)A 1999 37
- ANTS(ABN)A 1999 41
- ANTS(GST)A 1999 9-15
- ANTS(GST)A 1999 9-70
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- Brisbane City Council v. Valuer-General (Queensland) [1978] HCA 40; (1978) 140 CLR 41
- Collis v. FC of T (1996) 33 ATR 438; 96 ATC 4831
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- The Commonwealth of Australia v. Bogle (1953) 89 CLR 229
- The Trustee of the Estate of the Late AW Furse No. 5 Will Trust (1990) 21 ATR 1123; 91 ATC 4007

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- A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination (No. 2) 2000
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Schedule 1

A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination MSV 2005/3

I, Neil Edward Mann, make the following determination under subsection 75-35(1) of the *A New Tax System (Goods and Services Tax) Act 1999* ('the GST Act').

Citation

1. This determination may be cited as the *A New Tax System* (*Goods and Services Tax*) *Margin Scheme Valuation Requirements Determination* MSV *2005/3*.

Commencement

2. This determination commences on 1 December 2005.

Application of this Determination

3. This determination specifies the requirements for making valuations for calculating the margin for taxable supplies of real property made on or after 1 December 2005 for the purposes of Division 75 of the GST Act.

4. The *A New Tax System* (*Goods and Services Tax*) *Margin Scheme Valuation Requirements Determination* (*No. 1) 2000*, the *A New Tax System* (*Goods and Services Tax*) *Margin Scheme Valuation Requirements Determination* (*No. 2) 2000* and the *A New Tax System* (*Goods and Services Tax*) *Margin Scheme Valuation Requirements Determination* MSV 2005/1 continue to apply for supplies made before 1 December 2005, but do not apply to supplies made on or after 1 December 2005. The *A New Tax System (Goods and Services Tax) Margin Scheme Valuation Requirements Determination MSV 2* continues to apply in the circumstances specified in that determination.

What is the freehold interest, stratum unit or long-term lease that you value?

5. If the real property supplied is the same interest, unit or lease that existed at the valuation date, the valuation must be of that interest, unit or lease.

6. If the real property that is supplied is not the same interest, unit or lease that existed at the valuation date, but was derived from an interest, unit or lease that was in existence at that date, the valuation must be made as follows:

(a) a valuation of the interest, unit or lease in existence at the valuation date must be made; and

(b) the valuation of that interest, unit or lease must be apportioned on a fair and reasonable basis, to ascertain the part of the valuation that relates to the interest, unit or lease that you supply.

Mixed supplies

7. If you make a supply of an interest, unit or lease that is partly input taxed and partly taxable or partly taxable and partly GST-free (a mixed supply), the valuation must be made as follows:

(a) a valuation of the entire interest, unit or lease in existence at the valuation date must be made; and
(b) the valuation of that interest, unit or lease must be apportioned on a fair and reasonable basis, to ascertain the part of the valuation that relates to that part of the interest, unit or lease that you supply under the margin scheme.

The valuation methods that can be used for the purposes of Division 75

8. A valuation complies with the requirements determined by the Commissioner under subsection 75-35(1) if it is made in accordance with any of the following methods and is made by the time specified in paragraphs 15 and 16 below.

Method 1:

9. A written valuation by a professional valuer determining the market value of the interest, unit or lease at the valuation date. The valuation must be made in a manner that is not contrary to the professional standards recognised in Australia for the making of real property valuations.

10. The valuation must include a signed certificate which specifies:

(a) a full description of the property being valued;

(b) the applicable valuation date;

(c) the date the valuer provides the valuation to the supplier;

(d) the market value of the property at the valuation date;

(e) the valuation approach and the valuation calculation; and

(f) the qualifications of the valuer.

11. However, if:

(a) the interest, unit or lease has been supplied by the Commonwealth, a State or a Territory; and

(b) the supplier has held the interest, unit or lease since before 1 July 2000; and

(c) there were no improvements on the land or premises in question as at 1 July 2000; and

(d) there are improvements on the land or premises in question on the day on which the taxable supply takes place,

the valuation must be a valuation, made in writing by a professional valuer determining the market value of the interest, unit or lease, that is not contrary to professional standards recognised in Australia for the making of real property valuations, as if no improvements had been made at the date of the supply.

Method 2:

12. A valuation made by adopting as the value the consideration provided by a purchaser in a contract for the sale and purchase of the real property executed or exchanged before the valuation date by parties dealing at arm's length.

13. Method 2 is not available if:

(a) the interest, unit or lease has been supplied by the Commonwealth, a State or Territory; and

(b) the supplier has held the interest, unit or lease since before 1 July 2000; and

(c) there were no improvements on the land or premises in question as at 1 July 2000; and

(d) there are improvements on the land or premises in question on the day on which the taxable supply takes place.

Method 3:

14. A valuation made by adopting as the valuation the most recent value as determined before the valuation date by or on behalf of a State Government or a Territory Government department as the unimproved value, the site value, or the capital value of the land, for rating or land tax purposes.

When must the valuation be made?

15. The valuation must be made by the due date for lodgment of the supplier's Activity Statement for the tax period to which the GST on the supply is attributable.

16. However, if the Commissioner has allowed a further period under paragraph 75-5(1A)(b) for the supplier and recipient to agree in writing that the margin scheme is to apply in working out the GST on the supply, the valuation must be made by the later of:

(i) 6 weeks from the further period that the Commissioner has allowed under paragraph 75-5(1A)(b); or

(ii) 6 weeks from the date of the Commissioner's decision to extend the further period under paragraph 75-5(1A)(b).

17. If the valuation is not made within the time periods specified in paragraphs 15 and 16, the Commissioner may for good reason allow an additional period within which a valuation may be made.

Definitions

18. ***Professional valuer*** is defined for the purposes of this determination to mean:

(a) a person registered or licensed to carry out real property valuations under a Commonwealth, State or Territory law; or

(b) a person who carries on a business as a valuer in a State or Territory where that person is not required to be licensed or registered to carry on a business as a valuer; or

(c) a member of the Australian Property Institute and is accredited as a Certified Practising Valuer.

19. Other expressions in this determination have the same meaning as in the *A New Tax System (Goods and Services Tax) Act 1999*.

Dated this 7th day of September 2005

Neil Edward Mann
Deputy Commissioner and
Delegate of the Commissioner