GSTR 2010/D1 - Goods and services tax: interest-free loans received by the developer of a retirement village

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There is a Compendium for this document: **GSTR 2011/1EC** .

Generated on: 4 June 2026, 06:36:15 AM

Draft Goods and Services Tax Ruling

Goods and services tax: interest-free loans received by the developer of a retirement village

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Preamble

This publication is a draft for public comment. It represents the Commissioner's preliminary view about the way the law applies. It is not a public ruling or advice for the purposes of section 105-60 of Schedule 1 to the *Taxation Administration Act 1953*.

You can rely on this publication to provide you with protection from interest and penalties as follows. If a statement in this publication is later found to be incorrect or misleading and you make a mistake as a result of relying on this publication, you will not have to pay a penalty. In addition, if you have relied on this publication reasonably and in good faith you will not have to pay interest charges. However, you will still have to pay the correct amount of tax, provided the time limits under the law allow it.

What this Ruling is about

1. This draft Ruling considers the goods and services tax (GST) implications of interest-free loans (ingoing contributions) received by the developer of a retirement village tenanted under a 'loan/lease' arrangement.

2. In particular, this draft Ruling considers the relevance of ingoing contributions in determining:

- the consideration for the supply by sale of a retirement village to a purchaser; and
- the extent to which input tax credits are available for creditable acquisitions or importations[1] made by the developer to construct or develop the village,

for retirement villages that have the features set out in paragraph 13 of this draft Ruling.

3. Unless otherwise stated, all legislative references in this draft Ruling are to the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act).

[1] For the purposes of this draft Ruling, references to creditable acquisitions (Division 11) apply also to creditable importations (Division 15).

Date of effect

4. This draft Ruling represents the preliminary though considered view of the Australian Taxation Office (ATO). It may not be relied on by taxpayers or practitioners. When the final Ruling is officially released, it will explain our view of the law as it applies both before and after its date of issue.

5. The final Ruling will be a public ruling for the purposes of section 105-60 of Schedule 1 to 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 our view of when you can rely on our interpretation of the law in GST public and private rulings.

Transitional arrangements

6. Pre-existing arrangements for the development of a retirement village covered by paragraph 13 of this draft Ruling may be subject to transitional administrative treatment.

7. Goods and Services Tax Ruling GSTR 2004/9 currently sets out the Commissioner's views on the application of the GST Act where some or all of an entity's liabilities are imposed on or effectively assumed by the purchaser of the entity's enterprise. The Commissioner is currently reviewing the application of the principles in GSTR 2004/9 to retirement village arrangements and will clarify the scope of that ruling when this draft Ruling is finalised.

8. The Commissioner accepts that a reasonable interpretation of GSTR 2004/9 is that liabilities to repay ingoing contributions which are imposed upon the purchaser of a retirement village by statute are not included in the vendor's consideration for the supply of the village.

9. Accordingly, the developer of a retirement village will be permitted to apply the interpretation in paragraph 8 of this draft Ruling where it can be objectively determined that before the date of issue of this draft Ruling the developer became commercially committed to construct and develop a retirement village in accordance with the arrangement in this draft Ruling.

10. For these purposes, the Commissioner accepts that a commercial commitment exists where the developer has incurred or is contractually required to incur significant financial costs in relation to the construction and development of a retirement village through an arrangement covered by this draft Ruling. Such a commitment would exist, for example, where the developer has contracted to purchase land for the objective purpose of developing and constructing the village. However, these transitional arrangements will not apply merely because the developer has incurred costs before determining whether to construct and develop a retirement village (for example, by commissioning a feasibility study) or has entered into an option to purchase the land.

11. The transitional arrangement in paragraph 9 of this draft Ruling does not apply unless the developer's input tax credits are calculated on a consistent basis. This means that the transitional arrangement will not apply if the developer determines the extent of its creditable purpose using an output-based method which effectively recognises ingoing contributions as consideration for the supply of the village.

Class of arrangement

12. In this draft Ruling the term 'retirement village' has its general or industry meaning and is not limited to the statutory definition of 'retirement village' in section 195-1 of the GST Act.

13. This draft Ruling applies to arrangements that have the following features:

- An entity (the developer) acquires land on which it develops a retirement village (village).
- The developer enters into a residence contract with incoming residents in relation to a residential unit or apartment in the village (a 'unit').
- The unit is, or is intended to be, occupied as a residence or for residential accommodation.
- An amount (an 'ingoing contribution') is paid by the incoming resident to the developer to secure the right to reside in the village. The right to reside takes the form of a lease or licence (for convenience, 'lease') of extended duration.[2]
- The ingoing contribution is in the form of an interest-free loan. The developer is contractually obliged to repay the amount of the loan in full when the lease terminates.
- The village is then sold as a taxable supply (or as a GST-free going concern)[3] to another entity (purchaser) as 'new residential premises' within section 40-75.[4]
- The sale arrangement contemplates, either expressly or by implication, that the purchaser will be responsible for repayment of the outstanding ingoing contributions.

[2] For the purposes of this draft Ruling, references to tenancy include occupation under licence.
[3] Refer to Goods and Services Tax Ruling GSTR 2002/5 Goods and services tax: when is a 'supply of a going concern' GST-free?
[4] See also Goods and Services Tax Ruling GSTR 2003/3 Goods and services tax: when is a sale of real property a sale of new residential premises?

14. Commonly, the arrangements covered by this draft Ruling also have the following features:

- There are contractual or statutory requirements relating to the time and manner in which ingoing contributions are repaid.
- Repayment of the ingoing contributions is usually funded, in whole or in part, by money received by the operator of the village as ingoing contributions from incoming residents.
- Under the residence contracts, the operator of the village is entitled to receive certain amounts from the resident when the lease terminates or the resident leaves. These amounts can include:
  - deferred management fees based on the term of residence; and
  - an amount reflecting an agreed proportion of any decrease in the market value of the right to reside occurring during the outgoing resident's occupation.
- The developer may be liable to pay an outgoing resident an amount reflecting an agreed proportion of any increase in the market value of the right to reside occurring during the outgoing resident's occupation.
- The developer is entitled to set-off repayment of the ingoing contribution against the receipt of some or all of the amounts referred to above.
- In each State and the Northern Territory, legislation regulates the rights of outgoing residents to be repaid ingoing contributions.[5] In general terms, the effect of the legislation is to require the operator or owner of the village at the time of termination of the lease to repay ingoing contributions paid to a previous owner or operator of the village. Despite this, the legislation does not relieve the developer of its contractual obligation to repay ingoing contributions it has received.

[5] *Retirement Villages Act 1986* (Vic); *Retirement Villages Act 1999* (NSW); *Retirement Villages Act 1999* (Qld); *Retirement Villages Act 2004* (NT); *Retirement Villages Act 1992* (WA); *Retirement Villages Act 1987* (SA); *Retirement Villages Act 2004* (Tas).

Ruling

Consideration for the sale of a tenanted retirement village

15. In the circumstances in paragraph 13 of this draft Ruling, the purchaser provides the vendor with a benefit by assuming responsibility for repaying ingoing contributions received by the vendor which have not been repaid before the time of sale. The practical effect is that the vendor will not be required to repay the ingoing contributions it has received. For convenience, this benefit is referred to as the 'repayment benefit' in this draft Ruling.

16. The repayment benefit is included in the consideration for the supply of the village under the inclusive definition in section 9-15.

17. The repayment benefit is consideration which is 'expressed as an amount of money' within paragraph 9-75(1)(a). The 'amount' of money is the face value of the ingoing contributions received by the vendor which the purchaser assumes responsibility for repaying.

Determining creditable purpose or application

18. In the circumstances described in paragraph 13 of this draft Ruling the developer makes input taxed or GST-free leasing supplies[6] and a taxable or GST-free sale of new residential premises. It is therefore necessary for the developer to determine the extent to which its acquisitions have a creditable purpose.

Fair and reasonable method of apportionment

19. Acquisitions that relate only to making supplies that are taxable or GST-free are fully creditable. Acquisitions that relate only to making supplies that are input taxed are not creditable.

20. Development acquisitions relate to making taxable or GST-free supplies as well as input taxed supplies. These acquisitions are creditable to the extent that they do not relate to making supplies that would be input taxed. The extent of creditable purpose must be determined on a fair and reasonable basis.

21. Subject to paragraph 23 of this draft Ruling, the following formula represents a fair and reasonable method of calculating the extent of the developer's creditable purpose for development acquisitions:

$$\frac{\text{Estimated taxable or GST-free consideration}}{\text{Estimated taxable or GST-free consideration} + \text{Estimated input taxed consideration}}$$

[6] Section 40-35 and subsection 38-25(4A).

22. In this formula:

- 'Estimated taxable or GST-free consideration' means a reasonable estimate of all of the consideration the developer expects to obtain from:
  - the taxable or GST-free supply of the village; and
  - GST-free supplies of residential accommodation (if any), and
- 'Estimated input-taxed consideration' means a reasonable estimate of all consideration the developer expects to obtain from making input taxed supplies of residential premises in the village.

23. The formula in paragraph 21 of this draft Ruling represents a fair and reasonable method based on the arrangements addressed in paragraphs 13 and 14 of this draft Ruling. If additional circumstances exist, the fairness and reasonableness of using the formula would need to be assessed having regard to those circumstances.

Consideration for taxable and GST-free supplies

24. In this calculation, consideration for taxable or GST-free supplies includes the face value of ingoing contributions included in consideration for the supply of the village in accordance with paragraphs 16 and 17 of this draft Ruling. Ingoing contributions are only included in the apportionment calculation if, consistently with that approach, they are to be included in the calculation of the consideration for the supply of the village.

Consideration for input taxed supplies

25. Consideration for input taxed supplies includes the value of all benefits that the developer obtains from input taxed leasing of the village before sale. This includes the benefit of having access to the ingoing contribution amounts, interest-free. The period of the benefit begins on the date that the ingoing contribution is received and ends when it is repaid or when the village is sold,[7] whichever is the earlier.

26. This benefit can be valued by using a reasonable estimate of the additional financing costs the developer would incur over the relevant period if it borrowed an amount equal to the ingoing contribution under an arm's length interest bearing loan from a commercial financier. The Commissioner will accept a calculation that relies on the base interest rate used to calculate the general interest charge.[8]

[7] That is, at completion of the sale not entry into the contract of the sale.
[8] Subsection 8AAD(2) of the *Taxation Administration Act 1953*.

Fair and reasonable method of adjustment

27. Where the actual application of the developer's acquisitions differs from its reasonably estimated application, an adjustment under Division 129 is required.

28. Where the formula in paragraph 21 of this draft Ruling is used for apportionment, then the same method may be used for the purposes of Division 129 to calculate the extent of creditable purpose based on the actual application of the things acquired.

Other methods of apportionment or adjustment

29. A method other than that set out in paragraphs 19 to 28 of this draft Ruling can be applied where it provides a fair and reasonable basis of apportionment or adjustment.

30. An output based method which disregards the advantage of having interest-free loans is not fair and reasonable because it does not take into account all significant economic benefits obtained by the developer as a direct result of making input taxed supplies.

31. An 'effective life method', based on the time the developer holds the village for input taxed leasing, expressed as a proportion of an assumed overall 'effective life' for the village, is not fair and reasonable because it does not reasonably approximate intended or actual use by the developer.

Whether the repayment benefit is a creditable acquisition by the vendor

32. The repayment benefit is not a creditable acquisition of the vendor because it is not a supply to the vendor.[9] From the purchaser's perspective, the repayment benefit is not a supply which is separate from the repayment itself.

Explanation

33. The vendor of a retirement village with the features described in paragraph 13 of this draft Ruling either makes a taxable supply of new residential premises or a GST-free supply of a going concern.[10] The supply of a retirement village enterprise consists of the supply of real property, rights and other things that go to make up the retirement village enterprise. The supply of a village is not the supply of a revenue stream.[11]

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[9] Refer to paragraph 11-5(b).
[10] Section 38-325.
[11] See comment of Mason CJ in *Booth v. Federal Commissioner of Taxation* (1987) 164 CLR 159 cited at paragraph 34 of Goods and Services Tax Ruling GSTR 2004/4 Goods and services tax: assignment of payment streams including under a typical securitisation arrangement.

Consideration for the sale of a tenanted retirement village

34. The purchaser provides the vendor with a repayment benefit by assuming responsibility for repaying ingoing contributions received by the vendor. The practical effect of this benefit is that the vendor will not be required to repay those contributions.

The repayment benefit is consideration

35. The repayment benefit is considered to fall under the inclusive definition of 'consideration' in the GST Act because:

- The repayment benefit is a known and intended outcome of the supply arrangement.
- There is a contractual connection between the repayment benefit and the supply.
- The repayment benefit has a substantial relation in a practical business sense to the supply.
- The repayment benefit has an independent value and identity and is not merely an incidental aspect of the thing supplied or the process of supply.

The meaning of consideration

36. Subsection 9-15(1) defines 'consideration' on an inclusive rather than an exhaustive basis. Under that definition, 'consideration' includes the payments, acts and forbearances referred to in paragraphs 9-15(1)(a) and (b), as well as anything else which is 'consideration' for the purposes of general law.[12]

37. The purchaser's assumption of responsibility for the repayment of ingoing contributions is within the inclusive definition of 'consideration'[13] for the supply of the retirement village as that term has been interpreted by the courts in a revenue law context.[14]

[12] See, for example, *Currie v. Misa* (1875) LR 10 Exch 153 where Lush J stated that consideration may consist of 'some … responsibility, given, suffered, or undertaken… '.
[13] Subsection 9-15(1).
[14] *Archibald Howie Pty Ltd v. Commissioner of Stamp Duties (NSW)* (1948) 77 CLR 143 at 152; *Chief Commissioner of State Revenue (NSW) v. Dick Smith Electronics Holdings Pty Ltd* (2005) 221 CLR 496; 2005 ATC 4052; (2005) 58 ATR 241.

Known and intended outcome

38. Although consideration for a supply does not need to be given voluntarily, in the circumstances in paragraph 13 of this draft Ruling the repayment benefit is a known and intended outcome. The objective intention of the parties is that the vendor will receive the repayment benefit.

39. The objective intention of the parties is implicit in the fact that the supply proceeds on the basis that the vendor will not be required to repay the ingoing contributions it has received. That objective intention would also be expected to be reflected in the calculation of any other consideration provided in connection with the supply of the village.

Contractual connection

40. The purchaser's responsibility for the repayment of ingoing contributions may be in the form of an express requirement in the contract of sale. The presence of an express clause makes it clear that the repayment benefit constitutes part of the consideration for the supply of the village.

41. Alternatively, the contract may not contain any express clause regarding the repayment benefit. However, a term requiring the purchaser to repay ingoing contributions is likely to be implied into such a contract, on the grounds that such a term:

- forms part of custom or usage;[15] or
- is so obvious 'that it goes without saying';[16] and
- is necessary to give business efficacy to the contract.[17]

[15] *Con-Stan Industries of Australia Pty Ltd v. Norwich Winterthur Insurance (Australia) Ltd* (1986) 160 CLR 226 at 236-237.
[16] *Shirlaw v. Southern Foundries* (1926) Ltd [1939] 2 KB 206 at 227; *Codelfa Construction Pty Ltd v. State Rail Authority of New South Wales* (1982) 149 CLR 337 at 346-347.
[17] *Codelfa Construction Pty Ltd v. State Rail Authority of New South Wales* (1982) 149 CLR 337 at 346-347.

Substantial relationship

42. The repayment benefit has a substantial relation in a practical business sense with the supply of the village.[18] That relationship is sufficient to establish the repayment benefit as consideration for, or in connection with, the supply of the village. The concept of consideration under the GST is very broad and extends beyond the notion of consideration in contract law.[19]

43. The substantial relationship between the repayment benefit and the supply of the village is reflected in the fact that the repayment benefit forms part of the value passing which moves the supply of the village to the purchaser.[20]

44. The repayment benefit is of value to the vendor since the ingoing contributions are loans. A contractual promise to repay a particular amount of money in the future is legally a loan, whether or not it is given that label by the parties.[21] A loan is a presently existing debt of the borrower.

45. A payment by the purchaser to an outgoing resident does not merely discharge a statutory obligation of the purchaser (if any). It operates to effectively extinguish the vendor's contractual liability to repay the ingoing contribution and, as such, confers a real benefit on the vendor.[22]

Independent identity

46. The repayment benefit has a value and identity independent of the things supplied and of the supply arrangement.

47. An asset may carry an inherent burden or disadvantage which affects its value. A vendor of such an asset may not receive consideration merely because, by supplying the asset, it stops being exposed to that burden or disadvantage. In such a case, the burden or disadvantage is not consideration, because it lacks an identity which is independent of the asset.[23]

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[18] *Berry v. Federal Commissioner of Taxation* (1953) 89 CLR 653 at 659 per Kitto J.
[19] Explanatory Memorandum to A New Tax System (Goods and Services Tax) Bill 1999, at paragraph 3.9; *TT-Line Company Pty Ltd v. Commissioner of Taxation* [2009] FCA 658 at paragraphs 27-28.
[20] *Archibald Howie Pty Ltd v. Commissioner of Stamp Duties (NSW)* (1948) 77 CLR 143 at 152; *Chief Commissioner of State Revenue (NSW) v. Dick Smith Electronics Holdings Pty Ltd* (2005) 221 CLR 496; 2005 ATC 4052; (2005) 58 ATR 241.
[21] For example, *Richard Walter Pty Ltd v. Federal Commissioner of Taxation* 95 ATC 4440 at 4450; (1995) 31 ATR 95; *Re Securitibank Ltd (No. 2)* [1978] 2 NZLR 136 at 167; *Federal Commissioner of Taxation v. Radilo Enterprises Pty Ltd* 97 ATC 4151 at 4161; (1997) 34 ATR 635 at 646; see also, Taxation Ruling TR 2002/14 Income tax: taxation of retirement village operators, paragraph 29.
[22] Compare the treatment of a long-service leave liability by Wilson J in *Federal Commissioner of Taxation v. Foxwood (Tolga) Pty Ltd* (1981) 147 CLR 278; (1981) 11 ATR 859; 81 ATC 4261.
[23] See further, Goods and Services Tax Ruling GSTR 2001/6 Goods and services tax: non-monetary consideration, paragraphs 80 to 85.

48. However, the obligation to repay an ingoing contribution is a presently existing debt, recoverable as such at law. As such, it is not merely incidental to, or inseparably connected with, the assets comprising the retirement village.[24]

49. The obligation to repay ingoing contributions is separable from the village assets even if the liability is secured over the assets of the village. It is capable of being discharged while leaving the essential character of the village assets unchanged.[25]

50. Since the vendor's obligation to repay ingoing contributions has an independent identity, it follows that the purchaser's undertaking to repay those amounts also has an independent identity.

51. An incidental term or condition relating to the process of making a supply is not consideration. However, the repayment benefit does not represent a mere incidental term or condition. It arises from an understanding between the parties relating to the repayment of separately identifiable debts of significant value.

Amount of consideration

52. The purchaser's assumption of responsibility for repaying outstanding ingoing contributions is consideration which is 'expressed as an amount of money'. It is therefore monetary consideration.[26]

53. The 'amount of money' is the face value of the ingoing contributions received by the vendor which the purchaser assumes responsibility for repaying. Where the supply is taxable, that amount is included in the price of the supply.[27]

54. Not all monetary consideration need itself be money. 'Consideration expressed as an amount of money' is consideration that sounds in[28] or finds expression in money.[29] Such consideration is 'concerned only with' or has reference to 'the essential character of' money.[30] The purchaser's assumption of responsibility for repaying outstanding ingoing contributions satisfies these descriptions because it involves nothing more than the paying of monies in amounts which are known or readily quantifiable.[31]

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[24] *Swayne v. Commissioners of Inland Revenue* [1899] 1 QB 335 at 341. Since the obligation to repay an ingoing contribution is a debt, it is not akin to a liability that will arise in the future because of the continuation of an executory contract; compare with Goods and Services Tax Ruling GSTR 2004/9 Goods and services tax: GST consequences of the assumption of vendor liabilities by the purchaser of an enterprise, paragraphs 115-118.

[25] Compare: *Swayne v. Commissioners of Inland Revenue* [1899] 1 QB 335 at 341-342; see also, *Kemtron Industries Pty Ltd v. Commissioner of Stamp Duties* [1984] 1 Qd R 576 at 590.

[26] Paragraph 9-75(1)(a).

[27] Subsection 9-75(1).

[28] *Burrill v. Federal Commissioner of Taxation* (1996) 33 ATR 133; 96 ATC 4629.

[29] See GSTR 2001/6, paragraph 32.

[30] *Butterworth's Australian Legal Dictionary* Butterworths: Sydney, 1997. Also, Garner, B. *A Dictionary of Modern Legal Usage* Second Edition, New York: OUP, 1995.

[31] GSTR 2004/9, paragraphs 27-28.

55. It is not necessary that the amount of the ingoing contributions be explicitly referred to by the parties to the supply arrangement. Whether a benefit is 'expressed as an amount of money' does not turn on whether it has actually been ascribed a monetary amount or value.[32]

Determining creditable purpose or application

56. An entity is entitled to input tax credits for the creditable acquisitions it makes.[33] An acquisition is not creditable to the extent that it relates to making supplies that would be input taxed.[34]

57. In the circumstances described in paragraph 13 of this draft Ruling, the developer makes:

- input taxed supplies – comprising the leases of residential premises;[35] and
- one or more other supplies – including the taxable supply of the village as new residential premises[36] or supplies which are GST-free.

58. It is therefore necessary for the developer to apportion input tax credits for its development acquisitions by reference to its intended or planned use for the village[37] and to make adjustments under Division 129 to account for differences between the intended and the actual application of the things acquired.

59. The extent of creditable purpose and application must be determined on a fair and reasonable basis.[38] The basis of apportionment or allocation needs to make sense in the context of the enterprise and should not produce significant distortions.[39]

Reasonable method of apportionment or adjustment

60. Paragraphs 21 and 28 of this draft Ruling set out an apportionment and adjustment method which the Commissioner considers to be fair and reasonable, having reference to the arrangement within paragraphs 13 and 14 of this draft Ruling.

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[32] GSTR 2001/6 paragraph 40.
[33] Section 11-20.
[34] Paragraph 11-15(2)(a).
[35] Section 40-35.
[36] Paragraph 40-65(2)(b); section 40-75.
[37] See, for example, paragraph 17 of Goods and Services Tax Ruling GSTR 2006/4 Goods and services tax: determining the extent of creditable purpose for claiming input tax credits and for making adjustments for changes in extent of creditable purpose.
[38] See paragraph 49 of Goods and Services Tax Ruling GSTR 2008/1 Goods and services tax: when do you acquire anything or import goods solely or partly for a creditable purpose?
[39] See GSTR 2006/4 paragraph 121.

61. The method compares projected economic benefits obtained from leasing activities with projected economic benefits obtained from sale. This approach is an output based indirect method.[40] The premise behind methods of this kind is that expected economic benefits associated with an entity's acquisitions provide an objective measure of the purposes for which those acquisitions are used.

Consideration for taxable and GST-free supplies

62. Consideration for taxable supplies includes the amount of any ingoing contributions received by the vendor which the purchaser assumes the responsibility to repay. Objectively, this repayment benefit represents one of the advantages sought by the developer in making its acquisitions.

63. However, including this amount in the calculation of the developer's proportion of taxable supplies is not regarded as fair and reasonable unless that amount is also to be included in consideration for the supply of the village (for example, see paragraph 11 of this draft Ruling).

Consideration for input taxed supplies

64. In applying the formula referred to in paragraphs 21 and 28 of this draft Ruling, it is necessary to take into account all significant economic benefits obtained by the vendor from residents under the lease of their units prior to the date of sale.

65. These benefits are relevant to apportionment since they are advantages sought by the developer in making its acquisitions.

66. The advantage associated with obtaining access to ingoing contributions on an interest-free basis is also a benefit which is objectively sought by the developer.[41] As such, that advantage must be taken into account in determining the extent of creditable purpose and application.

67. The method referred to in paragraph 26 of this draft Ruling involves calculating the value of this benefit by reference to the cost of obtaining equivalent interest-bearing finance at arm's length. The Commissioner will accept a valuation which relies on the base interest rate used to calculate the general interest charge.[42]

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[40] See also paragraphs 120 and 143 to 153 of GSTR 2006/4 for a broad explanation and examples of this type of method.

[41] There is judicial support for the view that such an advantage is consideration for the supply of the premises by way of lease: *Customs and Excise Commissioners v. Exeter Golf and Country Club Ltd* (1979) 1 BVC 316; *Exeter Golf and Country Club Ltd v. Customs and Excise Commissioners* (1981) 1 BVC 385; *Commissioner for the South African Revenue Service v. Brummeria Renaissance (Pty) Ltd and others* (391/06) [2007] ZASCA 99; [2007] SCA 99 (RSA); [2007] 4 All SA 1338 (SCA) (13 September 2007).

[42] Section 8AAD of the *Taxation Administration Act 1953*.

Other methods of apportionment or adjustment

68. While other methods may provide a fair and reasonable basis of apportionment or adjustment,[43] there are some methods which the Commissioner considers are not fair and reasonable.

69. As explained in paragraph 61 of this draft Ruling, an output based method seeks to determine the advantages objectively sought by an entity in making acquisitions. Accordingly, such a method is not reliable if significant economic benefits directly associated with the use of those acquisitions are not taken into account.

70. For this reason, the Commissioner does not accept as fair and reasonable an output based method which does not reflect the benefit of the interest-free use of the ingoing contributions obtained from residents.

71. Input based methods are concerned with the actual use or consumption of acquisitions. Such methods are not reliable unless they reflect or reasonably approximate actual usage and application.

72. Accordingly, the Commissioner does not accept a method based on the time the developer holds the village for input taxed leasing expressed as a proportion of an assumed overall 'effective life' for the village.

73. Under this method, an apportionment might be determined by reference to the period for which the village is used to make input taxed supplies as a proportion of an assumed effective life for the village overall (for example, 40 years). That is, if the developer used the village for 5 years before selling, it might be assumed that 5/40ths of the investment has been used in making input taxed supplies.

74. Such a method contemplates the entire life span of the village rather than the actual use of the village by the developer. As such, it does not comply with the input tax credit provisions,[44] which are concerned with the use of a thing by a particular entity.[45]

75. An effective life method does not reasonably approximate such use as it is based upon an assumption of consistent use or consumption of acquisitions over time.

76. Such an assumption is problematic in the circumstances described in this draft Ruling, where there is the grant of a lease on terms which require the provision of a substantial interest-free loan at the commencement of the lease and the payment of deferred management fees on termination.

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[43] See generally, GSTR 2006/4.
[44] Refer Divisions 11 and 129.
[45] Refer Goods and Services Tax Ruling GSTR 2009/4 Goods and services tax: new residential premises and adjustments for changes in extent of creditable purpose, paragraphs 128-129.

77. Further, retirement villages include the land on which the relevant village is constructed. Land is generally an appreciating asset and the effective life of the relevant building is considered too remote and arbitrary to reasonably reflect the application of the residential premises comprising both the land and buildings during the relevant period.[46]

Whether the repayment benefit is a creditable acquisition by the vendor

78. The repayment benefit is not a creditable acquisition of the vendor because it is not a taxable supply to the vendor.[47]

79. From the purchaser's perspective, the acquisition of the village will require the future payment of money to residents. Viewed from that perspective, the undertaking to make the payment does not have an economic value or identity which is independent from the payment itself. The undertaking to repay ingoing contributions is not a supply in its own right, but is incidental to the payment which the purchaser will ultimately make.[48]

Alternative views

Alternative view 1

80. An alternative view is that, where the sale of the village occurs in an Australian State or the Northern Territory, the purchaser's assumption of responsibility for repayment of ingoing contributions is not consideration for the supply of the village.

81. According to this alternative view:

- The purchaser does not assume a liability to repay ingoing contributions, but has a liability imposed upon it. The purchaser's role is passive, and any mention by the parties of ingoing contributions merely reaffirms the operation of the legislation.
- Becoming subject to a statutory liability does not constitute a 'payment, act, or forbearance' by the purchaser or any other person.
- The vendor obtains no benefit from the purchaser repaying ingoing contributions because the payments discharge the purchaser's obligation rather than the vendor's.

[46] Refer GSTR 2009/4, paragraphs 128-129.
[47] Refer to paragraph 11-5(b).
[48] Refer GSTR 2004/9 at paragraphs 60 and 61.

82. This alternative view is not preferred because:

- The definition of 'consideration' is not exhaustive and extends beyond payments, acts and forbearances (see paragraphs 36 and 37 of this draft Ruling).
- The effect of the statute is a known and intended outcome of the arrangement described in paragraphs 13 and 14 of this draft Ruling and is connected to the supply of the village by contract (see paragraphs 38 to 41 of this draft Ruling).
- The repayment benefit has value to the vendor in a practical and business sense, whether or not the purchaser repays the ingoing contributions under a statutory obligation (see paragraphs 42 to 45 of this draft Ruling).

Alternative view 2

83. Another alternative view is that the repayment benefit is of minimal value to the vendor and should therefore be regarded as merely incidental to, rather than part of the consideration for, the supply of the village.

84. This view is based on the expected cash flow implications for a retirement village developer, bearing in mind that:

- the ingoing contribution is not repayable until termination of the lease;
- conditions relating to repayment of ingoing contributions are such that repayment would ordinarily coincide with or follow receipt of an ingoing contribution from a new resident; and
- in some cases, an outgoing resident may bear, in whole or in part, the risk that the ingoing contribution from a new resident will be less than their own ingoing contribution.

85. This alternative view effectively regards the vendor as having obtained substantially all the benefit of the ingoing contributions when entering into a lease.

86. The benefit of the ingoing contribution would be attributable to the input taxed leasing of units, rather than to the sale of the village, for the purposes of determining the extent of the developer's creditable purpose.

87. This alternative view is not preferred because it has insufficient regard to the fact that the ingoing contribution is a loan that is repayable by the developer. A liability to repay an ingoing contribution is a presently existing debt. It exists even though:

- there are contractual or statutory conditions which affect the timing of repayment;[49]
- it is likely that the developer will be able to fund the repayment by obtaining a new ingoing contribution; or
- the developer is able to repay all or part of its liability by way of set-off.[50]

88. This alternative view is also premised on the assumption that the developer would continue to lease units in the retirement village to residents and to use the cash flow from new ingoing contributions to fund repayment of outgoing residents. Such an assumption is not consistent with the arrangement described in paragraphs 13 and 14 of this draft Ruling.

89. A related alternative view is that any repayment benefit should be regarded as non-monetary consideration as it should be viewed in light of the practical benefit derived by the vendor rather than purely as a monetary benefit. It might be argued that the value of this practical benefit should be considered having regard to the features of the arrangement referred to in paragraph 84 of this draft Ruling. This view is not preferred because the ingoing contributions which the vendor benefits from not having to repay are an ascertainable, monetary amount.

Your comments

90. You are invited to comment on this draft Ruling. Please forward your comments to the contact officer by the due date.

91. A compendium of comments is also prepared for the consideration of the relevant Rulings Panel or relevant tax officers. An edited version (names and identifying information removed) of the compendium of comments will also be prepared to:

- provide responses to persons providing comments; and
- publish on the ATO website at www.ato.gov.au

[49] *Federal Commissioner of Taxation v. Citylink Melbourne Ltd* [2006] HCA 35; (2006) 62 ATR 648; 2006 ATC 4404 at 4426.
[50] By definition, a set off can only occur where there is a 'sum certain, immediately payable' against which a right may be offset: *Commissioner of Stamp Duties (NSW) v. Perpetual Trustee Co Ltd* (1929) 43 CLR 247 at 262-263.

Please advise if you do not want your comments included in the edited version of the compendium.

Due date:	**13 August 2010 (extended from 23 July 2010)**
Contact officer:	**Steven Iselin**
Email address:	**Steven.Iselin@ato.gov.au**
Telephone:	**(07) 3213 8417**
Facsimile:	**(07) 3213 8588**
Address:	**Australian Taxation Office PO Box 9977 CHERMSIDE QLD 4032**

Contact officer:	**Cheryl D'Amico**
Email address:	**Cheryl.D'Amico@ato.gov.au**
Telephone:	**(07) 3213 8158**
Facsimile:	**(07) 3213 8588**
Address:	**Australian Taxation Office PO Box 9977 CHERMSIDE QLD 4032**

Detailed contents list

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Commissioner of Taxation
9 June 2010

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Not previously issued as a draft

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Subject references:
- Goods and services tax
- GST retirement villages
- GST consideration

- GST input tax credits & creditable acquisitions
- GST new residential premises
- GST supplies & acquisitions

Legislative references:

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NO:	1-1RTQDTY
ISSN:	1443-5160
ATOlaw topic:	Goods and Services Tax ~~ Property and construction ~~ retirement villages