Revenue Law Journal

Volume 21 | Issue 1 Article 6

5-8-2012

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Recommended Citation

Tretola, John; Villios, Sylvia; and Callea, Pasqualina (2011) "GST and residential premises - which intention is relevant?," *Revenue Law Journal*: Vol. 21: Iss. 1, Article 6.
Available at: http://epublications.bond.edu.au/rlj/vol21/iss1/6

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# GST and residential premises - which intention is relevant?

**Abstract**
Sale of 'residences' normally do not attract capital gains tax, unless the sale is part of an enterprise. Australian courts have been inconsistent in interpreting the expression 'intended to be occupied and is capable of being occupied as a residence' in the GST legislation. This article explores whether a consistent approach has now emerged.

**Keywords**
Goods and Services Tax, GST, residence, residential premises, residential accommodation

This journal article is available in Revenue Law Journal: http://epublications.bond.edu.au/rlj/vol21/iss1/6

# GST AND RESIDENTIAL PREMISES - WHICH INTENTION IS RELEVANT?

JOHN TRETOLA* SYLVIA VILLIOS** PASQUALINA CALLEA***

Sale of 'residences' normally do not attract capital gains tax, unless the sale is part of an enterprise. Australian courts have been inconsistent in interpreting the expression 'intended to be occupied and is capable of being occupied as a residence' in the GST legislation. This article explores whether a consistent approach has now emerged.

## INTRODUCTION

The term 'residential premises' is defined in the *A New Tax System (Goods & Services) Act 1999* (GST Act)[1] as, amongst other things:

> land or a building that:
>
> (a) is occupied as a residence or for residential accommodation; or
>
> (b) is intended to be occupied, and is capable of being occupied, as a residence or for residential accommodation.

The meaning of the expression 'land or a building that ... is capable of being occupied as a residence or for residential accommodation' is important as it determines whether the supply of property will be input taxed, subject to GST as a taxable supply, or whether it will be GST-free. Australian courts have taken conflicting approaches in interpreting the expression 'intended to be occupied and is capable of being occupied as a residence'. This article explores how these approaches have diverged, and recently, converged into a more consistent approach that is accepted by both the courts and the Australian Tax Office.

We first consider the decision of the Federal Court in *Marana Holdings Pty Ltd v Commissioner of Taxation,*[2] where the Court took an objective approach to the meaning

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1 In s 195-1 of the *GST Act*.

2 (2004) FCA 233.

of the expression 'intended to be occupied as a residence'. We then consider the contradictory decision of the NSW Supreme Court in *Toyama Pty Ltd v Landmark Building Developments Pty Ltd*,[3] where the Court took the view that the subjective intention of the taxpayer was the appropriate test to apply.

Third, we consider the implications of the Full Court of the Federal Court's decision in *Sunchen Pty Ltd v Commissioner of Taxation*[4] and highlight how this case demonstrates a convergence in the law, by clarifying the expression *'intended to be occupied as a residence'*. The majority of the Full Federal Court decided this was to be interpreted according to an objective view of the facts, with the purchaser's subjective intention being irrelevant. We finally examine the approaches taken by some other tax jurisdictions such as those in New Zealand and the United Kingdom with respect to this issue.

## RELEVANT LAW

As noted above, s 195-1 of the GST Act defines the term 'residential premises' as 'land or a building that (a) is occupied as a residence or for residential accommodation, or (b) is intended to be occupied, and is capable of being occupied, as a residence or for residential accommodation'.

Subsection 40-65(1) of the GST Act provides that 'a sale of residential premises is input taxed, but only to the extent that the property is residential premises to be used predominantly for residential accommodation (regardless of the term of occupation).' Subsection 40-65(2) further provides that, 'the sale is not input taxed to the extent that the residential premises are: (a) commercial residential premises; or (b) new residential premises other than those used for residential accommodation.'

The term 'new residential premises' is defined in s 40-75 of the GST Act:

> (1) Residential premises are **new residential premises** if they:
>
> a. have not previously been sold as residential premises and have not previously been the subject of a long-term lease; or
>
> b. have been created through substantial renovations of a building; or
>
> c. have been built, or contain a building that has been built, to replace demolished premises on the same land.

Section 195-1 defines 'commercial residential premises':

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3 [2006] NSWSC 83.

4 [2010] FCAFC 138 (8 December 2010).

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

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

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

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

(e) a marina at which one or more of the berths are occupied, or are to be occupied, by ships used as residences; or

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

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

## ELEMENTS REQUIRED FOR A TAXABLE SUPPLY

Section 9-5 of the GST Act sets out the elements which are required for a supply to be a taxable supply. There must be a supply:

1. with consideration;
2. connected to Australia;
3. made by an entity registered or required to be registered for GST; and
4. made in the course or furtherance of an enterprise carried on by the entity.

Due to the need for a supply to be made in the course or furtherance of an enterprise, supplies of residential premises by private homeowners generally would not come within the scope of the Australian GST system, as, in most cases, individual homeowners are not selling their house as part of an enterprise. However, since the scope of what constitutes a transaction in the course or furtherance of an enterprise (as defined in s 9-20) is very wide, there is potential for the supply of used residential premises to be treated as supplies made in the course or furtherance of an enterprise. This raises a practical issue as to whether these supplies of residential property are input taxed or not.

## POLICY CONSIDERATIONS

GST is intended to be a tax on private consumption. However, in regard to the supply of residential premises for sale or rent, GST was not intended to be charged on established residential premises for sale or rent. This is set out in the Explanatory Memorandum to the GST Act, which provides that 'residential rents will be input-

taxed to ensure comparable treatment for renters with owner occupiers'.[5] The policy consideration behind treating supplies of used residential premises as input-taxed supplies is to keep a sound balance between taxing business inputs and ensuring that owners of residential premises need not concern themselves with any compliance difficulties arising from the GST treatment of such premises.[6]

Subject to satisfying all the elements for a taxable supply, the supply of new residential premises is a taxable supply.[7] Subsequent supplies of the property by enterprises are generally treated as input-taxed supplies. Therefore, the purchaser of new residential premises is not entitled to deduct the GST on the acquisition of the premises.[8] The GST paid by the original homeowner is passed on to subsequent owners because it remains an element of the price of the property.

The policy intent behind the GST Act is that used residential premises will only be input taxed to the extent that the premises are to be used predominantly for residential accommodation. For example, in a situation where a person supplies a shop with a flat above it, the supply of the shop will be taxable.[9] In addition, any value added upon conversion of 'commercial residential premises' into 'residential premises' is subject to GST.[10]

## KEY CASES ON THE MEANING OF RESIDENTIAL PREMISES

### 1. *Marana Holdings Pty Ltd v Commissioner of Taxation*[11]

In this case the taxpayer was a member of a partnership, registered for GST purposes, which appointed Tarfax Pty Limited ('Tarfax') as their agent. In May 2002, Tarfax, acting as this agent, entered into a contract for purchase to buy premises on which stood the 'Huntley Inn' ('the motel premises') for $5.7m. Included in the contract were certain plants and a restaurant. The contract was settled in September 2002

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5 Explanatory Memorandum to the A New Tax System (Goods and Services Tax) Bill 1998, Para 5.164; see also the judgment of the Full Court of the Federal Court of Australia (FCAFC) of 25 November 2004 in *Marana Holdings Pty Ltd v Commissioner of Taxation* (2004) FCAFC 307, and judgment of the Federal Court of Australia of 15 March 2004 in *Marana Holdings Pty Ltd v Commissioner of Taxation* (2004) FCA 233, paras 35, 36, 38, 197 and 198, and judgment of the New South Wales Supreme Court (Justice White) in *Toyama* [2006] NSWSC 83, para 95.

6 Exposure Draft of 10 April 2006 (as amended on 12 April 2006), Goods and Services Tax Treatment of Residential Premises, Explanatory Material, paragraph 1.5.

7 Section 9-5 of the GST Act.

8 Section 40-65 of the GST Act.

9 Explanatory Memorandum, see note 5.

10 Tax Laws Amendment (2006 Measures No. 3) Bill 2006, para 15.20 and example 15.4.

11 (2004) FCAFC 307.

when the land was conveyed to Tarfax. Until two days prior to settlement the property had been used as a motel.

In October 2002, the local Council approved a development application by Tarfax for the conversion of the motel premises into residential units. In December 2002, Tarfax entered into a building contract to renovate the motel premises so as to permit registration of a strata plan and sale of strata units. In February 2003, the building works were approved by an accredited certifier. The building work commenced in February 2003 and was finished in July 2003. Accordingly, room 202 in the motel premises became Lot 46 in Strata Plan 70815 and an existing car space became Lot 100 in Strata Plan 70815 (collectively 'Unit 46').

In August 2003, Tarfax entered into a contract to sell Unit 46 for $229,000 to Susan Anne Wells for use as residential premises. Settlement occurred in October 2003. The taxpayer argued that the sale of this home unit was the sale of residential premises to be used predominantly for residential accommodation - and so was an input taxed supply under s 40-65 of the GST Act - and that the premises were not new residential premises, as they had been sold previously to Tarfax in September 2002. Justice Beaumont in the Federal Court at first instance[12] held for the Commissioner, finding that the sale of Unit 46 was a taxable supply, as it was the sale of new residential premises.[13]

The taxpayer then appealed to the Full Federal Court.[14] It examined the expression 'new residential premises' and in so doing had to consider what was meant by the term 'residence'. Using the *Macquarie Dictionary* (revised 3rd edition), the word 'reside' was found to mean 'to dwell permanently or for a considerable time; have one's abode for a time'. Of the word 'residence' it states: 'the place, especially the house, in which one resides; dwelling place; dwelling; a large house; living or staying in a place of official or other duty'. The Full Federal Court therefore found that the terms 'reside' and 'residence' had a connotation of permanent or at least long-term commitment to dwelling in a particular place.

The Full Federal Court also noted[15] that the term 'residential' meant 'a dwelling serving or to be used as a residence in which one resides' and that therefore the word 'residential' had an aspect of permanent or long-term occupation.

Accordingly, the Full Federal Court held that the premises, when they were sold to Susan Wells, had the physical characteristics of property that supported its use as a

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12 *Marana Holdings Pty Ltd v Commissioner of Taxation* [2004] FCA 233 (15 March 2004).

13 Ibid para 33.

14 *Marana Holdings Pty Ltd v Commissioner of Taxation* [2004] FCAFC 307 (25 November 2004).

15 By reference to the *Oxford English Dictionary*.

residence. Therefore the sale was a taxable supply of new residential premises'.[16] In reaching this conclusion the Court held that the first sale of the premises as a motel to Tarfax was not the sale of residential premises, as the premises at that time could not be occupied as a residence and therefore the premises were 'commercial residential premises'. The Court also resolved that the subjective intention of the purchasers when they acquired the premises, which was to redevelop the premises and convert them to a strata title, was not relevant.[17]

### 2. *Toyama Pty Ltd v Landmark Building Developments Pty Ltd*[18]

Two entities (Toyama Pty Ltd and Landmark Building Developments Pty Ltd) as joint venturers acquired a property on 2 October 1998 that contained a free standing house that was divided into two self-contained residences.

The house on the property had at some point been used as a veterinary clinic and as a beauty therapist's business but had also been tenanted as residential accommodation until 20 August 2002. Development consent was obtained on 10 May 2000 from the local council to demolish the existing structures and to construct a 14-unit development and associated infrastructure on the land.

One of the entities, Landmark Building Developments Pty Ltd ('Landmark'), had entered into a joint venture with a trust, the KJR Family Trust ('the Trust'), in connection with this land development enterprise. On 10 September 2002 Toyama Pty Ltd ('Toyama') applied for an order for the appointment of trustees for the sale of the property. After obtaining relevant taxation advice it was determined that the sale of the property would be a taxable supply. The property was eventually sold at auction for $2.76 million on 7 August 2003.

A dispute then arose between the trustees and beneficiaries of the Trust as to whether GST was payable on the sale, particularly in view of the fact that the benefit of the plans and designs for the redevelopment would not pass to any purchaser.[19] It was the beneficiaries' view that the sale would not be a taxable supply but an input taxed supply of residential premises. The beneficiaries sued for breach of trust and claimed equitable compensation from the trustees for the erroneously applied amount of GST.

This trust dispute required the NSW Supreme Court, while not ordinarily being a court to resolve Commonwealth taxation disputes, to rule on the issue of whether GST did apply or not to the acquisition of the property in terms of the trust law issue.

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16 Ibid para 62.
17 Ibid para 67.
18 [2006] NSWSC 83 (28 February 2006).
19 Ibid para 26.

Justice White of the NSW Supreme Court ruled that the property in question was not to be used predominantly for residential accommodation.[20] Although the property in question had the physical characteristics of residential premises, such as bedrooms, a lounge room, a kitchen, bathrooms and a laundry, the supply of the property was a taxable supply because the purchaser 'did not intend to use the land and … buildings for residential accommodation. It intended to demolish the existing buildings.'[21]

In taking this view, Justice White indicated that a prediction as to the future use of the premises was required and that the most important factor in such a prediction was the intention of the future owner or lessee of the property.[22] His Honour noted that with a lease, the question as to how the property was to be used in the future would be determined by the terms of the lease. Conversely, in the case of a sale, it would depend upon the purchaser's intention, having regard to the objective circumstances such as the physical condition of the premises, the zoning or any restrictive covenants. Whilst his Honour noted that there would be practical difficulties in determining the vendor's liability for GST based on the intention of the purchaser, he thought this problem could be adequately resolved by careful drafting of terms in any sale contract to protect the vendor from any unexpected liability.[23]

Even if the matter was to be determined solely by objective criteria, his Honour concluded that this did not mean that the full range of available materials, including the subjective intention of the purchaser, should not be considered.[24] His view was that the subjective intentions of the purchaser taken with the objective criteria as a whole should be the applicable test. In applying that test to the dispute before him, his Honour ruled that the premises were not to be used predominantly for residential accommodation and so the sale by the trustees in 2003 was a taxable supply.

### 3. *Vidler v Commissioner of Taxation*[25]

This case was an appeal from a Federal Court decision.[26] It addressed the question of whether vacant land, which was zoned for residential purposes, could be treated as residential premises and thus input taxed.

The Full Federal Court determined that examining the physical characteristics of the properties, at the time of supply, was the relevant test in determining whether the

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20 Ibid para 101.
21 Ibid para 105.
22 Ibid para 92.
23 Ibid para 97.
24 Ibid paras 97 and 98.
25 [2010] FCAFC 59 (1 June 2010).
26 *Vidler v Commissioner of Taxation* [2009] FCA 1426.

premises were intended to be used predominantly for residential accommodation. Here, neither property contained shelter or basic living facilities and therefore could not qualify as residential premises because they were incapable of being occupied as a residence.[27] Therefore, the Court held that the properties could not be residential premises, no matter what their future intended use might be, and so the supply of each parcel of land was not input taxed.

### 4. *Sunchen Pty Ltd v Commissioner of Taxation*[28]

This case involved a GST-registered enterprise (with Sunchen Pty Ltd (Sunchen) being the trustee of the Sunchen Family Trust) carrying on business as a property developer.

Sunchen purchased a single-storey house with carport in 2006, subject to a residential tenancy. It claimed the GST on the purchase price ($47,807) as an input tax credit, on the basis that it did not intend to use the premises for residential accommodation but rather intended to develop the property into units for sale.

A development approval had been obtained by the purchaser to convert the property into a five-story residential group of apartments under a strata subdivision. Sunchen emphasised that it had a plan to develop the property within a short to medium term time frame.

Justice Perram of the Federal Court, at first instance,[29] held that the expression 'to be used predominantly for residential accommodation' in the GST Act directed attention to the objective circumstances of the premises and the use which can be derived from them. Interestingly, although Justice Perram did not agree with the approach taken by Justice White in *Toyama* (see above), his Honour would only depart from *Toyama* where it was 'clearly wrong'. His Honour noted, in any event, that White J did express a preference that required an objective assessment of the physical characteristics of the property at the date of acquisition.

The Full Federal Court, in the joint judgment of Edmonds and Gilmour JJ, expressly rejected the use of any subjective test, noting that there was nothing in s 40-65 of the GST Act which warranted such an approach and nothing which required a consideration as the future use by the purchaser.[30] Indeed, their Honours noted that using such a subjective approach would be entirely inconsistent with the fact that

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[27] In this case, the Full Federal Court followed the same reasoning as in its judgment of 20 November 2009 in *Steyne Hotel Pty Ltd v Commissioner of Taxation* [2009] FCAFC 155.

[28] [2010] FCAFC 138 (8 December 2010).

[29] *Sunchen Pty Ltd v Commissioner of Taxation* [2010] FCA 21 (29 January 2010).

[30] *Sunchen Pty Ltd v Commissioner of Taxation* [2010] FCAFC 138 (8 December 2010) paras 28 and 30.

GST liability was imposed on the vendor. A vendor would have no practical ability to challenge any resulting assessment by the Commissioner in any court or tribunal. To do so would require the court or tribunal to be persuaded as to the subjective intentions of a non-party to the proceedings.[31]

Furthermore, if the subjective intention of the purchaser were to be a relevant consideration, then this would raise the more difficult problem - when should this intention be assessed? It could either be at the time of acquisition, at the time of purchase, or some later time[32] Consequently, Edmonds and Gilmour JJ held that the relevant test to determine whether premises were residential premises or not in the context of s 40-65 of the GST Act was the physical characteristics or nature of the property at the time of the supply.[33]

Their Honours clarified that the words 'to be used predominantly for residential accommodation' did not refer to the use made by any particular person but rather to the attributes of the property to which its use was suited. However, this did not mean that the actual use made of the property would necessarily be irrelevant as 'the use to which an item is put would ordinarily be illustrative of at least some aspects of its character'.[34]

While the majority of the Full Federal Court (Gilmour and Edmonds JJ) held that the objective view represented the current law, Jessup J dissented on this point. His Honour took the view that the purchaser's intention would still remain 'an ingredient in the mix of facts' by reference to which a prediction was made as to the use to which the property was put.[35] These comments are unhelpful in resolving the question and cast doubt on whether this issue has been completely laid to rest.

## 5. *Travelex Ltd v Commissioner of Taxation* [36]

The High Court in *Travelex Ltd v Commissioner of Taxation* commented that the issue of subjective intention for the purposes of interpreting the GST Act was, at least for some purposes, a relevant consideration. The *Travelex* case did not deal with the specific issue of residential premises. Rather, the issue was whether a supply of foreign currency to a traveller leaving Australia was a financial supply and accordingly an input taxed supply, or whether the supply of foreign currency (as it

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31 Ibid para 32.

32 Ibid para 33.

33 Ibid paras 43 and 44.

34 Ibid para 41 quoting with approval the words of the Full Court of the Federal Court in *Hamilton Island Enterprises* (1982) 13 ATR 220.

35 *Sunchen Pty Ltd v FCT* [2010] FCAFC 46, para 7.0.

36 *Travelex Ltd v Commissioner of Taxation* [2010] HCA 33.

was supplied as part of the traveller's departure from Australia) was a GST-free supply.[37]

The critical issue to be resolved by the High Court was whether the supply of foreign currency on the departure side of Customs to a traveller leaving Australia was GST-free. This turned on whether the rights supplied were 'for use outside Australia'. Although the High Court was satisfied that the Fijian currency supplied was for use outside Australia, the High Court appeared to accept that whether the currency was for use outside Australia was primarily determined by the subjective intention of the recipient of the supply.[38] Nevertheless, the High Court acknowledged that, in taking this view, there would be practical difficulties in administering the relevant provisions if the recipient's intention needed to be considered.[39]

The *Travelex* case is an illustration of the presence of imprecise wording in the GST legislation, such as the ambiguous expression 'for use'. Here, in the context of supplies 'for use' outside Australia, interpretation proved difficult. This lends weight to the argument that there is a need either to redraft some of the GST legislative provisions or to define the term 'for use' in the GST Act more precisely to make it clear as to whether this expression is intended to be determined objectively or subjectively.

## DRAFT GST TAX RULING GSTR 2011/D2

The Draft GST Ruling issued on 5 August 2011 examines the meaning of the expressions 'residential premises' and 'commercial residential premises'. It also indicates that for premises to be 'residential premises', they should be used predominantly for residential accommodation.[40]

The Draft GST Ruling confirms the approach taken by the Full Federal Court in cases such as *Marana Holdings* and *Sunchen*. It states that the test to determine whether or not premises are residential premises for the purposes of ss 40-35, 40-65 and 40-70 of the GST Act is a single test that looks to the physical characteristics of the property - the subjective intentions of the purchaser are not relevant.[41]

The Ruling takes the view that the relevant test is to focus on the objective intention with which the premises were designed, built or modified and that this test requires

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37 Under item 4 of the Table in s 38-190 supplies of rights will be GST-free if they are supplied for use outside of Australia or to a non-resident who is outside of Australia when the thing supplied is done.

38 *Travelex Ltd v Commissioner of Taxation* [2010] HCA 33, paras 27-32.

39 Ibid para 36.

40 GSTR 2011/D2 para 6.

41 GSTR 2011/D2 para 6.

a focus on the physical characteristics of the premises in terms of their suitability for residential accommodation. Premises will be suitable for occupation as a residence if the premises possess features necessary for residential accommodation and are capable of being occupied as residential premises.[42]

Where the physical characteristics do not conclusively determine the suitability of the premises as a residence or for residential accommodation, then regard should be had to the design or construction documents, such as architectural plans, to determine whether the physical characteristics make the premises suitable for residential accommodation.[43]

If premises are in a dilapidated condition which prevents them from being occupied for residential accommodation, this would mean that the premises are not fit for human habitation and so are not capable of residential accommodation.[44]

If it is clear from the physical characteristics of the property that any suitability for the provision of living accommodation is ancillary to the prevailing function of the premises, then the Ruling takes the view that the premises are not residential premises to be used predominantly for residential accommodation.[45] The Ruling offers three examples involving an office building, a private hospital and a residential care facility. Although each of these provides some shelter and basic living facilities, they are not residential premises to be used predominantly for residential accommodation when considering their physical characteristics.

In the majority of instances, premises that possess characteristics suitable for residential accommodation will be used for that purpose. So, if the actual use made of the premises is for a purpose other than residential accommodation, this will not prevent the premises from being residential premises to be used predominantly for residential accommodation.

The Draft Ruling[46] adopts the joint decision of Edmonds and Gilmour JJ in *Sunchen*[47] and the approach taken by the Full Federal Court in the *Hamilton Island Enterprises case*.[48] The Draft Ruling also reinforces the view of the Commissioner of Taxation as expressed in his former GST Ruling[49] that the status of a property as residential property depends on its use based on the physical characteristics of the property.

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42 Ibid para 7.
43 Ibid para 8.
44 Ibid para 13.
45 Ibid para 15.
46 Ibid para 126.
47 [2010] FCAFC 138 (8 December 2010).
48 (1982) 13 ATR 220.
49 GSTR 2000/20.

## INTERNATIONAL TAX TREATMENT OF THE SALE OF RESIDENTIAL PREMISES

The Australian tax regime is consistent with the tax treatment of supplies of used residential property in many other parts of the world that have VAT-type taxes. For example, in New Zealand, the sale of used residential premises is treated as exempt from GST in specific circumstances.[50] These circumstances only apply where:

1. The property is sold in the course or furtherance of a taxable activity and was used by the supplier for the purpose of providing residential accommodation by way of rental, service occupancy agreement or licence; and
2. The property was used exclusively for that purpose for a period of not less than five years up to the date of sale.[51]

The Taxation Review Authority in New Zealand held in *S56*[52] that determination of the principal purpose of a dwelling involves considering both the subjective facts, including the purchaser's stated purpose, and the objective facts, including the actual, or reasonably anticipated, use of the property. An objective analysis of the use or intended use involves looking at an area breakdown of the property, or the relevant part of the property.

In Canada and the United Kingdom, supplies of used residential property are exempt.[53] However, in the United Kingdom, the supply of new residential property is not actually subject to VAT because the supply by the person who has constructed the property is zero rated.[54]

## UK MEANING OF 'DWELLING' - USE OF PROPERTY AT TIME OF SUPPLY TEST

In the UK the meaning of the phrase 'non-residential' is of considerable importance in obtaining zero rating when converting buildings into residential use under item 1(b) of Group 5 of Schedule 8 to the *VAT Act* 1994. The UK legislation, at Note 7 to Group 5 of Schedule 8, sets out the VAT meaning of 'non-residential' in the following terms:

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50 Section 14(1)(d) of the NZ *Goods and Services Tax Act 1985*.

51 The sale of a reversionary interest in land that was used by the supplier for the principal purpose of residential accommodation by way of rental, service occupancy agreement or licence would also be eligible for this exemption. However, s 14(1)(d) will not apply to the sale of property for the principal purpose of a taxable activity of property development where the principal purpose remains unchanged and continues to the date of sale.

52 TRA Decision of 14 June 1996 in *S56* (1996) 17 NZTC 7,361 and reported as TRA case 92/176 on p 40 of TIB (*Tax Information Bulletin*) Volume Seven, No 8.

53 Schedule V, Part 1 to the Canadian *Excise Tax Act 1985*.

54 Schedule 8, Group 5, Note 2 to the UK *Value Added Tax Act 1994*.

A building or part of a building is 'non-residential' if:

(a) it is neither designed, nor adapted for use-

a. as a dwelling or number of dwellings;

b. for a relevant residential purpose; or

c. it is designed, or adapted, for such use but -

i. it was constructed more than 10 years before the grant of a major interest; and

ii. no part of it has, in the period of 10 years immediately preceding the grant, been used as a dwelling or for a relevant residential purpose.

The House of Lords in *Uratemp Ventures*[55] took the view that the potential use of premises, having regard to all the circumstances of the case, was the relevant test. The case involved a hotel room that did not have any cooking facilities but did have the provision of a power point. This property was nevertheless held to be a dwelling (residential premises), as it was where the person lived and the room formed their principal home. Although the *Uratemp* case was not concerned with the VAT legislation directly (it concerned the definition of 'dwelling' under the *Housing Act* (UK) 1988), the case still set an important precedent regarding the meaning of what was residential premises.

In *Amicus Group*,[56] the VAT authorities relied on *Uratemp* in determining that bed-sitting rooms, which were the subject of conversion into flats, constituted dwellings. The Court held that, as they had been 'a place where one lives', the bed-sitting rooms were designed or adapted for use as dwellings.

However, the VAT Tribunal departed from this approach in *Kingscastle*,[57] which concerned the conversion of the upper two floors of a 400-year old coaching inn into three flats, where the ground floor and basement retained commercial use as a bar. The appellant argued that the decision in *Amicus* was incorrect, as there was not a 'use' requirement in the VAT legislation. The test was whether or not the property was 'designed or adapted for use as a dwelling'.

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55 [2001] 3 WLR 806.

56 *Amicus Group* [2002, No 17693].

57 Judgment of the Tribunal of 19 June 2002 in *Kingscastle Ltd* [2002, No 17777].

Therefore it was the design of the property that was important and not its use. The Tribunal accepted that, having been originally designed as a coaching inn with rooms to let, the inn was neither designed as a dwelling when it was originally constructed, nor had it been physically adapted for use as a dwelling since.

## UK TAX LAW - PHYSICAL CHARACTERISTICS OF BUILDING TEST

In the UK case of *Oldrings Development Kingsclere Ltd*[58] a self-contained building was built near the main house. This self-contained building contained a large room that was normally used as a studio, but occasionally the owner's children slept in it. There was a further small room with a toilet and wash basin, plus provision for a shower or bath. The VAT Tribunal decided that the building was a dwelling, as it could be used as a dwelling despite the fact that it did not have all the usual facilities.

In another case the University of Bath had constructed some buildings to be used as student accommodation. They were refurbished in three phases and, once refurbished; the buildings were all available for holiday letting. The VAT Tribunal held that the buildings were not dwellings because they were not to be used solely for relevant residential purposes.[59]

## SUMMARY ON MEANING OF 'RESIDENTIAL PREMISES' FOR GST PURPOSES

- The premises must be capable of being occupied as a residence and provide some basic living function, such as providing some element of shelter and basic living facilities such as a bedroom and bathroom, at the time the premises are supplied.[60]
- The relevant test to determine whether the premises were intended to be used predominantly for residential accommodation is to consider the physical characteristics of the property at the time of supply, and so vacant land could not qualify as residential premises because it was not capable of being occupied as a residence or for residential accommodation.[61]
- The words 'to be used predominantly for residential accommodation' do not refer to the use made by any particular person, but rather to the attributes of the property to which its use is suited. However, this does not mean that the actual use made of the property will necessarily not be relevant as 'the use to

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58 Decision of the VAT Tribunal of 23 May 2003 in *Oldrings Development Kingsclere Ltd v Commissioners of Customs and Excise,* VATTR 17,769 [2003] BVC 4,025.

59 *University of Bath v Commissioners of Customs and Excise* No 14,235 [1996] BVC 2,909.

60 *Vidler* [2010] FCAFC para 21.

61 Ibid para 34.

which an item is put will ordinarily be illustrative of at least some aspects of its character'.[62]

- The subjective intentions of the purchaser are not relevant, as the only relevant test for the purposes of s 40-65 is an objective test and is to be determined at the time of the supply based on the physical characteristics of the property and its present fitness for use in a particular way.[63]

## CONCLUSION

This article has considered the different methods used by the judiciary in Australia and other GST and VAT jurisdictions in characterising residential premises. The question of whether a supply of premises constitutes an input taxed supply of residential premises should be answered by considering objective criteria only. Such an approach will involve considering the physical characteristics of the property, as well as a number of other objective criteria. Any approach that involves considering the subjective intention of the purchaser is impractical and produces a result which is commercially unsound.

The view has been expressed that the provisions dealing with the various aspects of potential GST liability for 'residential premises' are found in 'a complex and difficult landscape in which the correct answer is not always self-evident'.[64] Another view mooted is that considering only the physical characteristics of the property at the time of supply is not enough. Consideration should also be given to other criteria, such as the location of the property, configuration of the site, any development consents for the construction of commercial premises and discussions between the parties leading up to the supply.[65]

While there is merit in both these viewpoints, there is no question that the Full Federal Court approach in *Sunchen*[66] has reduced the uncertainty and complexity over the definition of 'premises intended to be used for residential accommodation' by making it clear that the only relevant test is an objective test. The recently issued

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62 *Sunchen Pty Ltd v Commissioner of Taxation* [2010] FCAFC 138 at para 41 quoting with approval the words of the Full Court of the Federal Court in *Hamilton Island Enterprises* (1982) 13 ATR 220.

63 Ibid paras 63 and 68.

64 Robin Woellner, 'Wherever you hang your hat may be home, but is it 'residential premises' for GST purposes?' (2010) 3 *Journal of the Australasian Law Teachers' Association* 139, 153.

65 Sylvia Villios, 'Australian GST and residential property - uncertainty abounds' (2010) 21 (6) *International VAT Monitor* 426.

66 [2010] FCAFC 138 (8 December 2010).

Draft GST Ruling (GSTR 2011/D2) is a welcome step in the right direction to obtaining clarity on the issue.

It is hoped that there are still further improvements in this area of law. There is a compelling argument that some redrafting of some of the provisions of the GST legislation, such as s 40-65(1) and also the definition of residential premises in s 195-1, is necessary to either change the expressions used, or to make it clear which intention is relevant for each relevant section.