

**A National Tax Publication**

September 2006

## Tax Office compliance program released

The Tax Office recently released its Compliance Program for 2006-07. As with previous years' compliance programs, GST represents a significant aspect of the program. Interestingly, while GST revenue constitutes approximately 15% of all tax revenue collected by the Tax Office, collections from GST compliance activities make up approximately 25% of all compliance collections.

In keeping with its recent trend, the Tax Office proposes to further increase its GST compliance activities. The key GST issues identified by the Tax Office include:

- non-resident businesses that have a GST liability, but do not register for GST when they are required to do so;
- Australian businesses not charging GST to non-residents when required to do so;
- property arrangements that attempt to avoid or reduce GST payable; and
- timing schemes that accelerate and/or inflate input tax credit claims.

The Tax Office's proposed GST compliance activities tend to be more focused than in previous years. We summarise below the relevant issues for different business segments.

**Microbusinesses:** The Tax Office will focus on particular GST issues for microbusinesses (those with annual turnover of less than \$2 million). It will check

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that property developers are properly registered for GST. It will also target industries that are active in the cash economy, including building and construction, used motor vehicles, restaurants, cafes and take-away food outlets, licensed hotels and registered clubs, and horse racing. The Tax Office is also concerned that microbusinesses do not lodge activity statements on time and do not hold satisfactory records to justify the amounts contained in their returns.

**Small to medium enterprises:** For the 2006-07 year, compliance with GST obligations is a major focus for businesses in the SME segment (those with annual turnover between \$2 million and \$100 million). In particular, it will review businesses that have undertaken public share floats to ensure input tax credits were not overclaimed on float expenses. It will also conduct reviews and audits of small to medium enterprises that deal with real property. These reviews will examine non-compliance with GST obligations in areas such as sales, professional valuations and calculating change in the extent of creditable purpose. The Tax Office is also concerned that infrequent and complex transactions, such as financial supplies, are often not reported correctly for GST purposes. *Continued over page...*

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**Large businesses:** In 2004-05, the Tax Office's GST compliance activities raised over \$350 million in GST liabilities from large businesses (those with annual turnover greater than \$100 million). The 2006-07 program highlights a number of GST issues for large businesses. The Tax Office will monitor large GST refunds claimed by businesses to ensure they are valid. It will review property transactions involving the margin scheme, in particular, ensuring that valuations are not excessive and comply with the law, that the margin is correctly calculated and that change of use adjustments are made where required. The Tax Office will also focus on issues concerning financial supplies, such as supplies of services to associated entities at less than market value, recovery of GST on costs relating to mergers and acquisitions, and ensuring businesses are using fair and reasonable GST apportionment methodologies.

In addition, the Tax Office is concerned that some large businesses have failed to keep their internal corporate governance processes and systems for GST up to date. Examples include transactions processed outside of the accounts payable or accounts receivable systems not being classified correctly, incorrect GST formula defaults or GST codes, and failure to update GST capture and reporting systems when other business systems are changed.

**Non-profit entities:** Non-profit entities often have complex GST issues. However, many are not familiar with their tax obligations. The Tax Office's compliance program recognises that non-profit organisations often have limited resources and expertise to understand and comply with their record keeping responsibilities. The Tax Office will focus on continuing to develop strategies to improve these organisations' understanding of the GST rules for non-commercial supplies, such as accommodation and meals.

**BDO comment:** The latest compliance program highlights how serious the Tax Office is about GST compliance. Given the Tax Office's policy of ordinarily imposing penalties and interest on GST mistakes, it is crucial that businesses have good GST risk management practices in place. Appropriate practices include training for relevant staff, drafting and updating a GST policy manual, and regular review of internal and external GST systems and procedures.

These practices make it more likely that errors will be identified and also demonstrate GST compliance to the Tax Office in any audit. We recommend you contact your local BDO indirect tax expert if you would like to discuss appropriate GST risk management practices for your business.

## GST & retirement villages



In August the Commissioner issued draft GST Ruling GSTR 2006/D3, which discussed retirement village premises and use of communal facilities. The draft Ruling discusses when the provision of "communal facilities" within or in connection with a retirement village will be considered to be the supply of care services and accommodation in relation to a retirement village. Community facilities recognised by the Commissioner include such things as a library, dining room, recreation room, pool or barbeque area.

In the Commissioner's opinion, "communal facilities" must be "physical" (therefore, they are not services provided to residents) and must be provided within, attached to, or connected with the residential buildings or constructed on surrounding land. Additionally, they must be provided for the primary purpose for the communal use of residents, although it does not need to be for their exclusive use nor does there need to be any evidence that the residents actually use the premises. *Continued over page...*

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**BDO comment:** While some readers may wonder why the Commissioner has devoted resources to considering such an esoteric concept as the definition of “communal facilities”, those readers in the retirement village sector will understand the importance of this concept. In 2004, amendments were made to the GST law to ensure that supplies of care services and accommodation within a retirement village were GST-free, as opposed to being input-taxed (as residential accommodation) or subject to GST. One of the requirements for premises to

be classified as a “retirement village” is that the premises include some communal facilities. This draft Ruling is the Commissioner’s first step in clarifying what that means.

It is interesting to note that “communal facilities” do not include services or other intangibles provided to residents. Nor do they include in-room services (they are not “communal”) or off-site services. It will be necessary for retirement village operators to review their facilities to ensure that they will fulfil this requirement for the retirement village to be GST-free.

## Tax Office publishes view of *Toyama*

Readers might recall the concerns raised by the NSW Supreme Court decision in *Toyama Pty Ltd v Landmark Building Developments Pty Ltd* [2006] NSWSC 83. The Tax Office has now responded to the case by deciding to ignore it.

The *Toyama* decision raised some difficult GST issues for property developers, in particular, that the vendor of a property had to take account of the purchaser’s likely use of the property when determining the GST classification of the sale (refer the April 2006 edition of this GST News). This would have the result that many sales of existing residential property by registered businesses to property developers would be taxable, even though this appears to be contrary to the policy of the GST law for residential property.

The Tax Office has now responded to the *Toyama* decision. The Tax Office disagrees with the decision, which is contrary to the view published in GST ruling, GSTR 2000/20. Accordingly, the Tax Office will continue to administer the provisions in accordance with the views in GSTR 2000/20 pending further judicial clarification.

**BDO comment:** The Tax Office’s response is odd to say the least. It has effectively decided to ignore a court decision that it considers incorrect. Clients should be careful about relying on court decisions that conflict with Tax Office opinions. As was seen with the recent amendments to the GST residential property rules, the Government is prepared to ignore or retrospectively amend the GST law where the outcome of a GST case is not to its liking. Going forward, readers should carefully consider their contracts for the sale of existing residential premises to ensure they are not adversely impacted by these developments.



## GST documents released in August

In August there were a number of Releases issued concerning GST. One of the more interesting on a theoretical level was the comment by the Assistant Treasurer in Parliament that, for the 2004-05 income year, approximately 275,000 businesses with a turnover less than \$50,000 were registered for GST purposes and paid GST. One can only surmise that such businesses find that the ability to collect input-tax credits and pass-on the GST to consumers is more economical than absorbing the GST in their inputs, thereby outweighing the compliance burdens of collecting and paying GST.

There was also a short Administrative Appeals Tribunal case on GST, *Vadasz and Commissioner of Taxation* [2006] AATA 682. The Tribunal found against the taxpayer due to its poor GST records, providing a warning to all other taxpayers to keep their books in order.

The documents relevant for GST include:

- *Tax Laws Amendment (2006 Measures No 5) Bill 2006*, which was introduced into Parliament in August (it contains amendments ensuring cars and pharmaceuticals are GST-free for certain Defence Force personnel and persons on certain Disability Pensions);
- *A New Tax System (Goods and Services Tax) Simplified GST Accounting Methods Determination 2006/1*, which provides a simplified GST accounting method for restaurants and cafes (this was followed by a Treasurer's press release of 15 August, discussing this method);
- Addendum to GST Ruling GSTR 2004/9 (which discusses the GST consequences of the assumption of vendor liabilities by the purchaser of an enterprise);
- Addendum to GST Ruling GSTR 2006/7 (which discusses the application of the margin scheme to a supply of real property made on or after 1 December 2005 that was acquired or held before 1 July 2000);
- Addendum to GST Ruling GSTR 2006/8 (which discusses the application of the the margin scheme for supplies of real property acquired on or after 1 July 2000);
- Erratum to GST Ruling GSTR 2006/5 (discusses the meaning of the term "Commonwealth, a State or a Territory");
- Interpretive Decision ATO ID 2006/202 (GST and acquisition of legal tender for possible re-sale as collectable coins and notes);
- Interpretive Decision ATO ID 2006/203 (GST and foreign currency export); and
- ATO media release No 2006/30, titled "Jail sentence for activity statement fraud".

In addition, the Tax Office withdrew an Interpretive Decision in relation to GST and hospital treatment. If readers would like more details of any of these documents, please contact the BDO office in your State.

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