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WEEKLY COMMENT: THURSDAY 24 MARCH 2016

1. Last week I looked at the determination of the date of acquisition of land under s. CB 15B. This week I consider some issues relating to determining the date of disposal of land. I also consider the time of supply of land for GST purposes.

Section CB 15B does not apply to determine the time of disposal of land

2. Section CB 15B does not apply to determine the date on which land is disposed of for income tax purposes. This view is supported by the fact that in the Exposure Draft of Public Ruling – BR Pub 14/08 *Income tax – Timing of disposal and derivation of income from trading stock* issued after the new rule was enacted, it was stated that:

“The Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Act 2014 has inserted a new s CB 15B in the Act, which deals with when land is acquired. The new section has implications for when land is disposed of.”

3. However, this statement was not included in the final version, and there is no authoritative statement by Inland Revenue, which suggested that the rule in section CB 15B applies to disposals.
4. Furthermore in Draft Question We’ve Been Asked *Income tax – Date of acquisition of land* (“the draft QWBA”), which I reviewed last week, it is stated in paragraph 10 that:

“It is noted that the date at which land is acquired for the purposes of the land provisions in subpart CB will, in most cases, not be the date at which it is disposed of by the vendor. This QWBA does not consider the date of disposal of land.”

The date of disposal of land

5. From a vendor’s point of view, the relevant date is the date on which income is derived, which in most cases will be the date of disposal. The better view is that this will be the settlement date. The following points are made in Inland Revenue’s Question We’ve Been Asked “When does derivation occur in relation to land sales with a deferred settlement, by business taxpayers who provide vendor finance?” published in *Tax Information Bulletin* Vol. 16, No. 5, June 2004, pages 34-40:

(a) The general principles of derivation are the same for land, goods and services.

(b) The case of *FC of T v Australian Gas Light Co* 83 ATC 4800 is significant as it acknowledges that if further steps are required before the taxpayer is entitled to sue for a debt after a

"sale" has taken place, then derivation will only occur once those steps have been taken and the taxpayer is able to sue for the debt.

- (c) The Commissioner considers that the judgments in *Gasparin v FCT* (1994) 94 ATC 4, 280 and *Ruddenklau v Charlesworth* [1925] NZLR 161 support the concept of derivation, in relation to a sale of land, generally occurring when there is an enforceable debt (which is different from there being an ability to sue for specific performance) and that this is generally the same time as the vendor loses their dispositive power over the property.
 - (d) In some cases this will be when the unconditional contract is signed. In other cases it will be at the time of settlement. It is necessary to look at what is intended in the contract and all the facts and circumstances. Both *Gasparin* and *Ruddenklau v Charlesworth* support the proposition that derivation occurs at settlement.
 - (e) In *Gasparin*, the judge held that income was derived at the time of settlement (not when the contract became unconditional), when a debt accrued due from the purchaser to the taxpayer - it was held that the time when the debt arose was the critical consideration.
 - (f) In *Ruddenklau v Charlesworth* it was stated that, as a general rule, on the failure or refusal of a purchaser to complete an executory contract for the purchase of land the vendor is not entitled to sue for the purchase money as a debt, he is entitled merely to sue for specific performance or for damages for the loss of his bargain, and it is only when the contract has been completed by the execution and acceptance of a conveyance that unpaid purchase money may become a debt and can be recovered accordingly.
6. The final version of Public Ruling – BR Pub 14/08 “Income tax – Timing of disposal and derivation of income from trading stock” was published in *Tax Information Bulletin* Vol. 26, No. 10, November 2014, pages 17-25. The discussion there relates to trading stock. The exposure draft referred to earlier in paragraph 2 above stated that “Land is generally not trading stock, except in certain circumstances, and the ruling now does not include land”. This statement is not included in the final version.
7. In BR Pub 14/08, two situations are distinguished between:
- (a) If trading stock is disposed of in the ordinary course of business, it is the time of “derivation” of income that is relevant – i.e. when a legally enforceable debt arises (which seems to be consistent with the discussion above); and
 - (b) If trading stock is sold outside the ordinary course of business, or to put an end to the business or part of it, it is the date of “disposal” that is relevant, which will be the date the parties intended the goods to pass if a clearly expressed intention is evident from the terms of the contract, or there is no clearly expressed intention, according to the statutory rules in section 20 of the *Sale of Goods Act 1908*, which could be the date the contract becomes unconditional, if there is an unconditional contract for specific goods in a deliverable state, otherwise when any actions required are completed.
8. In the case of the land, in general, there would be a clearly expressed intention that the goods are to pass upon settlement. The case of *Australian Gas Light* provides support for the view that a disposal will not occur until settlement. The comments on the statutory rules regarding intention in s. 20 of the *Sale of Goods Act 1908* in BR Pub 14/08 relate to trading stock, so the conclusions may not be of direct relevance.

9. Therefore, the timing of a disposal of land will generally coincide with the timing of derivation of income and be on the settlement date. In order to determine whether any of the sale proceeds will be taxable income, there are a number of taxing provisions in subpart CB (as discussed last week), each of which must be considered in turn.

Time of supply for GST purposes

10. For GST purposes, under s. 9(1) of the *Goods and Services Tax Act 1985* (“the GST Act”), a supply of land is deemed to take place at the earlier of the time an invoice is issued by the supplier or the recipient or the time any payment is received by the supplier, in respect of that supply.
11. For GST purposes, the sale of land comprises a single supply, not a series of supplies depending on when the various interests in the land change hands. In *TRA 88/196 v C of IR* [1989] NZTRA 69; *Case L67* (1989) 11 NZTC 1,391, the judge stated:

“This case relates to the timing of the payment of GST. I find that GST on the full sale price must be made at the outset – in this case, the day the auction and signing of contract and payment of deposit, rather than some months later when title is available and the vendor is able to collect the balance of the purchase price from the purchaser of the section. ...

From the outset there is a binding contract for the supply of a section, and enforcement rights pass to the purchaser. Only performance of the contract, or final implementation, is delayed until title is available. The conditions in the contract do not affect its substance. There is contractual certainty. ... I do not think that it matters that the deposit is paid for title to a section, but that only a chose-in-action is made available at time of payment of deposit. The different interests (equitable at first and later legal) do not alter the commercial reality that, when the deposit was paid, a section of land was acquired; the transaction was unlikely to be frustrated or avoided; and only routine conveyancing steps needed to be completed.”

12. The single supply will take place, under s. 9(1) at the earlier of the time an invoice is issued by the supplier or the recipient or the time any payment is received by the supplier. Conditional and unconditional agreements for the sale and purchase of property will not constitute invoices for the purposes of the GST Act. It is stated in IS 07/02 “Is an agreement for the sale and purchase of property an “invoice” for GST purposes?” *Tax Information Bulletin* Vol. 19, No. 7, August 2007, pages 7 – 15 that:

“It is concluded that a conditional agreement for sale and purchase of property will not constitute an “invoice” for the purposes of the Act. Also, it is concluded that a conditional agreement for the sale and purchase of property that becomes unconditional will not constitute an “invoice” for the purposes of the Act. Therefore, a conditional standard form agreement for sale and purchase of property will not trigger the time of supply — even if the conditional agreement becomes unconditional.

It is also concluded that unconditional agreements for the sale and purchase of property will not constitute “invoices” for the purposes of the Act. Therefore, the formation of an unconditional agreement for the sale and purchase of property will not trigger the time of supply.”

13. In relation to when “any payment is received by the supplier” a deposit is sufficient – as stated in *Case L67* referred to in paragraph 11 above. It is stated in IS 10/03 “GST: time of supply – Payments of deposits including to a stakeholder” published in *Tax Information Bulletin* Vol. 22, No. 6, July 2010 that:
- (a) A deposit constitutes “any payment”. Where a supplier receives a deposit under a contract, the time of supply will be triggered under s. 9(1). This applies equally to conditional or unconditional contracts.
 - (b) Where a deposit is paid to a person as stakeholder, there will have been no receipt by the supplier and the time of supply will not be triggered. A supplier may be a stakeholder.
 - (c) A stakeholder relationship requires agreement by all parties. A person cannot declare himself or herself a stakeholder unilaterally. A stakeholder holds the deposit on behalf of both parties and owes a contractual or quasi-contractual obligation to both parties. The intention of the parties, determined from all the circumstances, will establish in which capacity a person receives a deposit.
14. It can be seen that Inland Revenue accepts that a deposit paid under a conditional contract to a stakeholder, such as a real estate agent or the vendor’s solicitor, will not constitute a “payment” that triggers the time of supply.
15. Following *CIR v Dormer* (1997) 18 NZTC 13,446 Inland Revenue accepts that a supplier can be a stakeholder – it does not necessarily have to be an independent third party. However, it requires agreement by all parties, as noted above.
16. Inland Revenue also states that:
- “If the third party stakeholder pays or applies the payment to the supplier or for the supplier’s benefit during the period of the stakeholding in error. ... for example, where the stakeholder mistakenly believes the relevant event has taken place (such as the contract becoming unconditional) or the stakeholder accedes to a unilateral request by the supplier ... As the supplier is not acting in any stakeholder capacity, the supplier will have received payment for the purposes of section 9(1). ...
- If the supplier as stakeholder is entitled to the interest and the interest is applied to the purchase price, the interest will constitute a payment received by the supplier in respect of the supply and the time of supply will be triggered.”
17. Inland Revenue also considers the situation where a contract (signed or not) constitutes a non-binding contract. (e.g. where there is no firm commitment on the part of either party to the arrangement). An initial payment made under such a contract might not constitute a payment in respect of any future supply. Inland Revenue states that:
- “ ... the legal arrangements between the parties must be considered in determining whether a supply exists ... a supply need not necessarily be made under a contract. The crucial question is not whether there is a contract, but whether there is a supply. In the absence of a binding contract there is no automatic assumption of a transaction giving rise to a supply. It is necessary, therefore, to consider whether there has in fact been a supply that is chargeable with GST. Has the payment received been made for a supply? ...

The cases emphasise the necessity for reciprocal obligations between the parties. If a supply cannot be connected to the payment by reciprocal obligations, it cannot be said the payment is consideration for the supply. There must be reciprocal obligations between the parties to make payment and to make a supply of goods or services for the payment. A payment made merely in the hope that a supply would be made is not sufficient to constitute consideration."

18. Inland Revenue summarised the position where there is no binding contract as follows:

"Where there is no binding contract, it must be shown that the payment is for the supply of goods or services, whether the physical supply takes place now or in the future. Where this is the case, the receipt of the payment by the supplier will trigger the time of supply."



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