

# Legal Decisions <sup>(21)</sup>

*Goods and services tax - input tax - purchase of farm property with a dwelling - whether purchaser of farm property can claim input tax credits for full purchase price - whether definition of input tax anticipates apportionment - principle purpose of making taxable supplies - Goods and Services Tax Act 1985, ss2(c), 5(14) and 10(18).*

## IN THE COURT OF APPEAL OF NEW ZEALAND

CA 237/94

BETWEEN THE COMMISSIONER  
OF INLAND REVENUE

Appellant

AND NEIL WILLIAM COVENEY and  
CAROLE ALISON COVENEY

Respondents

BETWEEN THE COMMISSIONER  
OF INLAND REVENUE

Appellant

AND JOHN FRANCIS DOOLEY

Respondent

BETWEEN THE COMMISSIONER  
OF INLAND REVENUE

Appellant

AND NANCY PRICILLA SWAIN and  
JOHN WAYNE ADAMS

Respondents

Coram: Richardson J  
Gault J  
Blanchard J

Hearing: 18 May 1995

Counsel: J R Eichelbaum and Mrs  
Barbara Corbett for Appellant  
D E McLay for Respondent

Judgment 25 May 1995

### **JUDGMENT OF THE COURT DELIVERED BY RICHARDSON J**

This appeal from a judgment of Fraser J reported at (1994) 16 NZTC 11,328 concerns the apportionability of consideration paid on the purchase of farm property in arriving at the input tax credit under the Goods & Services Tax Act 1985 where the purchasers are registered but the vendors are not registered persons for gst purposes.

### **The factual background**

The 3 cases before the court are representative of different factual situations but they have common features. Each was a purchase of a farm property. While each farm had a building occupied and used as a dwellinghouse, the dwelling had not been subdivided off. In each case the agreement provided for sale of the property as a single undivided unit and for a single sum. In short, the agreements actually entered into and carried out neither contemplated nor allowed as between the parties for apportionment of either the subject matter or the consideration. That was the position as between the parties to each transaction.

For 2 reasons purchasers may decide to make an apportionment for their own purposes. First, under the Stamp & Cheque Duties Act 1971 a dwellinghouse is exempt from conveyance duty and s24(2) explicitly provides for an apportionment to arrive at the value of the dwellinghouse (including curtilage). Second, for financial reporting and income tax purposes farmers traditionally apportion the purchase price between land and buildings. But those practices do not change the legal character of the preceding transaction between vendor and purchaser.

In each case the purchaser claimed an input tax deduction in respect of consideration paid on the purchase. The Commissioner disallowed that part of the deduction referable to the valuation for stamp duty purposes of the house and curtilage. The factual differences were that in one case (Coveney) the portion of the value attributed to the house was less than 50% of the consideration for the purchase of the property and the house was leased out; in the second (Dooley) the position was the same but the house was lived in by the purchaser; and in the third (Swain and

Adams) the land was used intensively for their horse training business but the portion of the value attributed to the house was over 50% of the consideration paid for the property. However, it is now common ground that nothing turns on any of these factual differences.

### **The legislation**

Under the Goods & Services Tax Act goods includes all kinds of personal or real property (s2(1)) and the resale of land is a sale of "secondhand goods". The statute imposes a tax on the supply of goods and services. The supply of residential accommodation is exempt. Registered persons collect and account for gst on goods and services supplied by them but are entitled to deduct amounts charged by way of gst on goods and services supplied to them. An input tax credit is also available in some circumstances in respect of secondhand goods even though no gst is payable by the supplier because he or she is not registered for gst purposes. It is this provision (para (c)) and the proviso of the definition of input tax in s2 which is in point in the present case. That definition reads as follows:

"Input tax", in relation to a registered person, means

- (a) Tax charged under section 8(1) of this Act on the supply of goods and services made to that person;
- (b) Tax levied under section 12(1) or section 13(1) of this Act on goods entered for home consumption under the Customs Act 1966 by that person;
- (c) Any amount equal to the tax fraction (being the tax fraction applicable at the time of supply within the meaning of section 9 or any other provision of this Act) of the consideration in money for the supply, being a supply by way of sale that is not a taxable supply, to a registered person of any secondhand goods situated in New Zealand -

being in any case goods and services acquired for the principal purpose of making taxable supplies:

Provided that where, in relation to any supply to which paragraph (c) of this definition applies, the supplier and recipient are associated persons, or the supply is not the only matter to which the consideration relates, the consideration in money for that supply shall, for the purposes of this definition, be deemed to be the lesser of the purchase price or the open market value of that supply."

The second limb of the proviso "or the supply is not the only matter to which the consideration relates" was inserted by s2(2) of the 1989 Amendment Act.

Various provisions of the legislation in their terms contemplate apportionment. Mr Eichelbaum for the Commissioner relies particularly on s5(14) and s10(18). Section 5(14) anticipates that a single supply may be charged for tax in part under s8 (where the 12½% rate applies) and in part under s11 (where the zero rate applies). Section 5(14) provides:

"For the purposes of this Act, where a supply is charged with tax in part under section 8 of this Act and in part under section 11 of this Act, each such part shall be deemed to be a separate supply."

Section 10 is concerned with taxable supplies and so relates to supplies by registered persons and subs (18) provides:

"Where a taxable supply is not the only matter to which a consideration relates, the supply shall be deemed to be for such part of the consideration as is properly attributable to it."

### Decision of Fraser J

The argument for the Commissioner in the High Court was that the definition of input tax expressly and by necessary implication contemplates apportionment. Fraser J concluded that the supply was of the farm as a whole. Although the farm comprised land, buildings and a dwelling, none of the items could be dealt with separately and in each case there was a single supply of the property sold, not a multiple supply of its component parts. It followed that the pro-

viso to para (c) did not assist the Commissioner because, if there was only one supply, that was the only matter to which the consideration related. Sections 5(14) and 10(18) both dealt expressly with taxable supplies where apportionment of one sort was clearly contemplated but a different regime applied to input tax in respect of secondhand goods which did not constitute a taxable supply. The test under the definition of input tax was whether the property had been acquired for the principal purpose of making taxable supplies. That carried with it the recognition that there are, or may be, subsidiary purposes which do not include the making of taxable supplies. Fraser J found, and it is no longer in issue, that the principal purpose of each taxpayer in acquiring the particular property was to make taxable supplies, the principal purpose being to run the property as a business venture.

### The Commissioner's arguments on appeal

In its essentials the Commissioner's argument was that, adopting a purposive and workable construction of the legislation reflected in the parallel provisions of s5(14) and s10(18), apportionment was required on the present facts under the input tax definition. Mr Eichelbaum submitted that the facts could properly be analysed in 3 ways, any one of which would justify the Commissioner's apportionment approach:

- (1) There were 2 supplies, one of the land used for business purposes and the other of the dwelling and adjacent land.
- (2) Without resort to the proviso, para (c) should be read as calling for apportionment: the input tax is referable to the consideration for the supply of secondhand goods in so far as they are acquired for the principal purpose of making taxable supplies.
- (3) Applying the proviso, the supply was not the only matter to which the consideration related: expanding the phrase by incorporating the earlier qualifying expression so as to read "the supply of **goods acquired for the principal purpose of making supplies** is not the only matter to which the consideration relates", the other matter here was the provision of domestic accommodation.

The short answer to the first proposition is that the legal character of the transaction between vendor and purchaser as entered into and carried out was "a supply by way of sale", to use the words of para (c), of a single property for a single consideration. It was that undivided property which was supplied as an entirety by the vendor to the purchaser. From the perspective of the purchaser the acquisition of the property served 2 purposes, that of making taxable supplies and of providing housing accommodation. But that does not change the true character of the supply from the vendor to the purchaser.

In answering the second and third questions it is important to set particular provisions in their statutory context and to accord them a purposive interpretation. But we must give due effect to the scheme and language of the particular provision, here para (c) and the proviso. In that regard s5(14) is against rather than for the Commissioner's proposed reading of the input tax definition provision. It is a deeming provision: each part of a single supply is deemed to be a separate supply. As a possible parallel, s10(18) is more in point. It uses the same formula as under the proviso "a [taxable] supply is not the only matter to which the consideration relates". Where that test is met s10(18) provides that "the supply is deemed to be for such part of the consideration as properly attributable to it". That has been regarded as allowing apportionment of farm property sales between registered persons. In that situation there is of course symmetry of gst treatment between vendor and purchaser. And the correctness of that practice is not an issue in this case.

Paragraph (c) and the proviso must be read according to their natural and intended meaning. The difficulty facing Mr Eichelbaum's second proposition is that para (c) does not contain any language indicative of or allowing for apportionment. On the contrary the input tax is the "amount equal to the tax fraction ... of the consideration in money for the supply". As under (a) and (b), it is a calculable sum and the yardstick then applicable in each case is whether or not the subject matter of the supply was "acquired for the principal purpose of making taxable supplies". If the principal purchase test is satisfied, the

full amount is the applicable input tax. Further, the proviso itself proceeds on the premise that, subject to the operation of the proviso, the full amount is the applicable input tax.

The third proposition is equally unsupported when tested against the proviso. The proviso applies where, and only where, "the supply is not the only matter to which the consideration relates". To come within the proviso it is necessary to identify a matter, other than the supply in question, to which the consideration relates. Thus, on a sale of land with late settlement, the consideration may contain an interest equivalent component which may fairly be described as a second matter to which the consideration relates. No doubt other examples could be given. The point is that there are circumstances where, giving the words their ordinary and natural meaning, the proviso could have effect. It follows that there is no basis in the scheme and language of para (c) and the proviso for invoking the proviso where the consideration does not relate to any matter other than the supply of secondhand goods which has already satisfied the principal purpose test. There may be sound policy reasons for apportioning the consideration on the sale of farm property and other secondhand goods and whether or not the vendor is a registered person. But for the reasons given we are satisfied that to do so on the present facts would be inconsistent with the scheme and language of the input tax definition.

The appeal is dismissed. Although a test case we see no justification for interfering with Fraser J's decision that costs simply follow the event rather than being fixed on a solicitor-client basis as submitted for the respondents. However, a higher than the usual party-party award is appropriate in respect of the appeal given that the Commissioner having lost in the High Court put these respondents to the expense of an appeal and the tax in dispute for all 3 is under \$30,000. Costs on the appeal are fixed at \$10,000 together with all reasonable disbursements as fixed by the Registrar.

**Solicitors:**

Crown Law Office, Wellington, for the Appellant

Bell Gully Buddle Weir, Wellington, for the Respondents