



6 April 2009

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Draft Interpretation Statement IS3571: Retirement Villages – GST Treatment.

1. The Society's Taxation Committee (the Committee) is grateful for the opportunity to comment on the IRD reissued draft interpretation statement *Retirement Villages – GST Treatment (17 February 2009) (Interpretation Statement)*.
2. The Committee supports the publication of an interpretation statement to assist the retirement village industry in dealing with these difficult GST issues. We acknowledge that the Commissioner has made significant amendments to the draft interpretation statement issued on 25 July 2007. The Committee supports the majority of those amendments. However, in the Committee's view, the interpretation statement is still deficient in a number of areas, most notably in its analysis of the meaning of "appurtenances". The Committee does not support the publication of the interpretation statement in its present form.
3. This submission is structured as follows:
 - 3.1 First, we set out our views on how the Interpretation Statement should operate when it is eventually finalised. In particular the Interpretation Statement should apply only to arrangements entered into after it is issued.
 - 3.2 Secondly, we set out our concerns with the analysis of the meaning of "appurtenances" in the definition of "dwelling". Paragraphs 47 to 60 of the Interpretation Statement use selected case law to support the view that any area that a resident of a dwelling has a "right to use" must be appurtenant to the dwelling. This is not the correct test.
 - 3.3 Thirdly, we summarise our views on how the test for apportioning exempt and taxable supplies should apply to a retirement village.
4. All statutory references are to the Goods and Services Tax Act 1985, as amended, ("the Act").

Transitional Provisions

5. It is likely that significant transitional issues will arise when the Interpretation Statement is finalised, as the Interpretation Statement reflects a change in Inland Revenue policy. Given the delay in finalising the Interpretation Statement and the complexity and uncertainty that exists in this area of law, any changes in policy should apply only prospectively. Further, given the uncertainty that has surrounded the GST treatment of retirement villages, the Commissioner should not impose shortfall penalties or use of money interest on retirement villages that have previously adopted a tax position consistent with earlier draft Interpretation Statements, but inconsistent with any final Interpretation Statement.
6. If a retirement village is required to adopt a different tax position following the issue of a finalised Interpretation Statement, then it is likely that any resulting costs will be passed on to residents. Therefore, any final Interpretation Statement should apply only to arrangements entered into after the date the final Interpretation Statement is issued. The Commissioner adopted a similar approach with respect to Interpretation Statement 07/02- "Is an agreement for sale and purchase of property an "invoice" for GST purposes?" which applied only to agreements entered into on or after 1 July 2007.
7. The Inland Revenue Department has recently released a Discussion Document - "Options for strengthening GST neutrality in business-to-business transactions" (June 2008), which contains proposals to re-define a "dwelling" and a "commercial dwelling". The Interpretation Statement should not be finalised until the proposals contained in the Discussion Document are dealt with, as the Interpretation Statement will need to be revised if there are any changes to the definition to "dwelling" and "commercial dwelling".

The Meaning of "Appurtenances"

8. As stated above, the analysis set out in the Interpretation Statement on the meaning of "appurtenances" is flawed.
9. The meaning of "appurtenances" is relevant to determining what is included in the exempt supply of accommodation in a "dwelling". A "dwelling" is defined in section 2 of the Act as:

"any building, premises, structure, or other place, or any part thereof, used predominantly as a place of residence or abode of any individual, together with any appurtenances belonging thereto and enjoyed with it; but does not include a commercial dwelling."
10. The Committee does not agree with the Commissioner's view that the right to use common areas and facilities is an appurtenance. The Act imposes three requirements in order for land to be treated as an "appurtenance" and therefore part of a "dwelling" for GST purposes:
 - (a) The land must be an appurtenance;
 - (b) The appurtenance must be "belonging thereto" (the dwelling);
 - (c) The appurtenance must be "enjoyed with it" (the dwelling).

11. The Interpretation Statement should apply all three of these legislative requirements in determining whether or not an area of land is appurtenant to a dwelling, rather than using the broader ‘right to use’ test.
12. Further, the meaning of “appurtenant” should not extend to an area that is geographically distant from a resident’s individual dwelling. Only land that is within the curtilage of a dwelling can be an appurtenance to the dwelling. In *Case M64* (1990) 12 NZTC 2,363, Bathgate DJ noted that an appurtenance would “normally apply only to the land upon which the dwelling stood, and that, perhaps, immediately adjacent thereto”.
13. *Norfolk Apartments Ltd v CIR* (1995) 17 NZTC 12,212 reviewed the relevant case law on the meaning of “appurtenance”. These cases confirm that the term “appurtenance”, in respect of a dwelling that is a house, should be given its natural meaning and could not be extended to land outside the curtilage of the house. The cases referred to in *Norfolk* remain good authority in New Zealand and were only distinguished in *Norfolk* on the facts. The decision in *Norfolk* does not automatically apply to any area within a retirement village complex to which residents of a dwelling have a “right to enjoy”, particularly where those areas are geographically distant and completely separate from the dwelling.
14. In Example 1 of the Interpretation Statement (Paragraphs 113-118), the Commissioner sets out an example of a retirement village with 200 stand-alone villas, 50 apartments and various common facilities which all residents have a right to use. The Interpretation Statement concludes that the common facilities are appurtenances of the villas and therefore part of the exempt dwellings for GST purposes. The Committee submits that in a retirement village of 200 stand-alone villas, most of the villas will be geographically distant from the common facilities because of the large size of the village. Case law does not support the Commissioner’s contention that an appurtenance can be geographically distant from a dwelling and still be treated as part of the dwelling. Further, Example 1 fails to consider whether the appurtenances are “belonging thereto and enjoyed with” the dwellings, as required by the Act.
15. Based on relevant case law, only land adjacent to a dwelling can be “appurtenant” to a dwelling. Land, or the right to use land, which is geographically distant from a dwelling cannot be “appurtenant” to the dwelling. The Commissioner should revise the meaning of “appurtenance” in the Interpretation Statement accordingly.

Input Tax Adjustments – Common Areas and Facilities

16. Paragraph 108 of the Interpretation Statement proposes that the extent to which common areas and facilities are used for making taxable supplies and exempt supplies should be determined based on the number of units that are commercial dwellings relative to the number of units that are dwellings. The Committee suggests that a better way to apportion the use of common areas and facilities would be the revenue generated from dwellings relative to revenue generated from commercial dwellings. A revenue-based test would be more consistent with the manner in which the principal purpose test applies.
17. Other methods of apportioning the taxable and exempt use of the common areas and facilities could, in certain circumstances, also produce a fair and reasonable result (e.g. apportionment based on costs incurred or land area). The Interpretation

Statement should make it clear that retirement villages are free to choose any apportionment method that is fair and reasonable in the village's circumstances.

Examples

18. The Commissioner's GST treatment of common areas and facilities in Example 1 could be considered wrong for the reasons set out in paragraph 14 above.
19. The inclusion of additional examples in the Interpretation Statement would be of assistance to the retirement village industry.

The committee trusts these comments are helpful. If you require further assistance please do not hesitate to contact Diana Brown, the committee secretary, by phone (04) 463-2967 or email diana.brown@lawsociety.org.nz

Yours sincerely

A handwritten signature in black ink, appearing to read 'S Tomlinson', with a stylized flourish at the end.

Stephen Tomlinson
Co-Convener, Taxation Committee