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QWB00078 – Goods and services tax – non-profit bodies – registration, accounting for GST, and de-registration

Introduction

1. The New Zealand Law Society (Law Society) appreciates the opportunity to comment on draft Question We've Been Asked QWB00078, *Goods and services tax – non-profit bodies – registration, accounting for GST, and de-registration* (the draft QWBA).

Comments

Supply of donated goods and services

2. Paragraph 26 of the draft QWBA considers the GST treatment of the supply of donated goods and services. The Law Society agrees with the analysis set out in the draft QWBA. However, it would be helpful if the Commissioner affirmed (or otherwise) her policy that where the sale of goods by a non-profit body comprises both donated goods and/or services and goods and/or services that have been purchased, the Commissioner will consider that the supply is an exempt supply of donated goods, provided that the cost of the purchased goods and/or services is less than 5% of the sale price of the goods (see IRD Technical Rulings Manual, paragraph 104.6.5).
3. The Law Society appreciates that taxpayers have been advised that the material contained in the IRD Technical Rulings Manual should not be relied upon as representing Inland Revenue's current views or practice (letter from Tony Bouzaid, National Manager, Operations Policy, 2 September 1998), but notes that the Commissioner has not provided any subsequent guidance on what constitutes a donated good or service. The draft QWBA provides an opportunity for the Commissioner to provide such guidance.

Apportionment of input credits

4. Paragraph 32 of the draft QWBA notes that where a non-profit body uses goods or services partly for making exempt supplies (e.g. the supply of donated goods stored in a building), then "... some apportionment will be needed on input tax claimed ...". The Law Society considers it would be helpful if the draft QWBA set out the basis for making such an apportionment (i.e. that it is up to the registered person to determine how the apportionment should be made, but that the method adopted must provide a fair and reasonable result – see section 20(3G) of the Goods and Services Tax Act 1985).

Adjustments on registration

5. Paragraph 33 of the draft QWBA states an adjustment can be made for goods or services acquired before the non-profit body became GST registered, but only if "[t]he goods or services ... have been charged with GST...". Section 21B of the Goods and Services Tax Act 1985 has been amended so that an adjustment can also be made in respect of the acquisition of second-hand goods. Paragraph 33 implies that no adjustment can be made in respect of second-hand goods acquired before a non-profit body becomes GST registered, which is not correct.

Adjustment where use changes to total taxable or total non-taxable use

6. Paragraph 34 of the draft QWBA deals with the "wash-up" calculation under section 21FB of the Goods and Services Tax Act 1985 where the non-profit body's use of goods or services changes to 100% taxable or 100% non-taxable use. The last sentence of paragraph 34 states that if the requirements set out in section 21FB are met, then "the organisation will be able to make this adjustment in the second adjustment period" [emphasis added]. Presumably, the inclusion of the words "will be able to" is intended to convey to the reader that such an adjustment cannot be made earlier. However, the Law Society is concerned that the use of the words "will be able to" implies that it is not mandatory to perform the "wash-up calculation". The Law Society recommends that the wording of the last sentence of paragraph 34 is reworded to read "... the organisation is required to make this adjustment in the second adjustment period" [emphasis added].

Deemed supply of goods and services forming part of taxable activity on deregistration

7. Paragraphs 45 and 46 of the draft QWBA deal with the GST output tax liability arising on the deemed supply of goods and services forming part of the assets of a taxable activity on deregistration under section 5(3) of the Goods and Services Tax Act 1985. The extent of this liability will turn on: (i) the identification of the taxable activity carried on; and (ii) a determination of what goods and services are part of that taxable activity.
8. Paragraph 21 of the draft QWBA notes that the definition of "taxable activity" in section 6(1)(a) of the Goods and Services Tax Act 1985 requires that the activity "in whole or in part" involves or is intended to involve the supply of goods and services to another person for a consideration, and that it follows that a "taxable activity" is not confined to the activity connected with making supplies for consideration, but can be a broader activity, carried on continuously or regularly, where only part of the activity involves making supplies for consideration.

9. Paragraph 22 of the draft QWBA concludes that, in the fact situation under consideration, hiring out the hall “forms part of the organisation’s wider activity of providing community assistance and education, and raising funds for that purpose”. The Law Society is concerned that the Commissioner has not correctly identified the activity carried on by the non-profit body and has confused the organisation’s purpose with its activities.
10. Put simply, the “purpose” of the non-profit organisation referred to in the draft QWBA is to provide community assistance and education, and the means by which it achieves that “purpose” is to solicit donations of goods, services and money, derive income by hiring out its facilities and to provide free programmes and events to the community. Each of these “means” involves the organisation undertaking one or more separate activities.
11. The inclusion of the words “in whole or in part” in section 6(1)(a) of the Goods and Services Tax Act 1985 does not enable these separate activities to be treated as a “wider activity” just because those activities relate to a common purpose. On the contrary, the Law Society considers that the reference to the words “in whole or in part” are intended to refer to a situation where an activity (e.g. hiring a hall) is carried on partly to make supplies for a consideration (e.g. rental at a charge), and partly for other purposes (e.g. rental to community groups at no charge or for the organisation’s own use).
12. The Law Society is also concerned with the Commissioner’s use of the word “and” to combine a number of disparate activities into a “wider activity”. Taken to its logical conclusion, the Commissioner may consider that a church body that hires out its hall to community groups is carrying on the “activity” of “providing religious and community services”, with the result that the church body will be required to account for GST on such assets as its church building, silverware, church organ and church pews on deregistration, even though the church body may not have claimed back GST on these assets (particularly if they were acquired prior to registration), and those assets have nothing whatsoever to do with the church body’s activity of hiring out its hall to community groups.
13. The Law Society wonders if the reason the Commissioner has taken such an expansive view of the meaning of the term “taxable activity” is because the Commissioner is concerned that non-profit bodies could claim back GST on all goods and services not acquired to make exempt supplies under section 20(3K) of the Goods and Services Tax Act 1985, but not account for GST when those goods or services are subsequently supplied (including on deregistration). The Law Society acknowledges that the application of section 20(3K) could give rise to that outcome, as section 20(3K) deems such goods and services to be acquired to make taxable supplies, but does not deem those goods and services to be part of the non-profit body’s taxable activity.
14. The Law Society does not, however, consider that the best approach to deal with this asymmetry is to take a strained approach to determining the taxable activity actually carried on by the non-profit body. One possible solution may be to amend section 20(3K) so that it applies for GST output tax purposes as well (by deeming all goods and services acquired by a non-profit body, other than goods and services acquired as part of an exempt activity, to have been acquired for the non-profit body’s taxable activity). A better solution, however, may be to enact a deemed supply rule in section 5 of the Goods and Services Tax Act 1985 to the effect that if a non-profit body claims back GST on a good or service, then the subsequent supply by that non-profit body of that good or service (on deregistration or otherwise) is

deemed to be a taxable supply. An amendment to that effect has previously been proposed to section 5(16) of the Goods and Services Tax Act 1985 in relation to dwellings.

Adjustment for deemed supply of goods or services on deregistration

15. Paragraphs 47 and 48 of the draft QWBA deal with the GST adjustment under section 21F of the Goods and Services Tax Act 1985 on deregistration. Paragraph 48 states that, on the facts set out in the draft QWBA, no adjustment is likely under section 21F because "... the organisation will likely have claimed a full input tax deduction for the hall under s 21FB when it registered for GST" [emphasis added]. The Law Society is concerned that the use of the words "when it registered for GST" implies that the section 21FB adjustment can be made immediately after registration. That is not correct as such an adjustment can be made only at the end of the second adjustment period after the change of use.

Conclusion

16. This submission was prepared with assistance from the Law Society's Tax Law Committee. If you wish to discuss this further please do not hesitate to contact the committee convenor Neil Russ, through the committee secretary Jo Holland (04 463 2967, jo.holland@lawsociety.org.nz).

Yours faithfully

A handwritten signature in black ink, consisting of a stylized initial 'C' followed by a long horizontal line.

Chris Moore
President