

GST treatment of bodies corporate

A government discussion document

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CHAPTER 1

Background

- 1.1 New Zealand's Goods and Services Tax (GST) rules require businesses, clubs and other entities to register for GST if they supply goods or services worth more than \$60,000 a year. GST-registered persons are required to file GST returns and pay GST on the goods and services they provide (their supplies). The amount of GST they pay is based on the value of these supplies less the GST cost of any inputs that they purchase from other GST-registered persons. In this respect the GST system only taxes the "value added" by each business in a supply chain.
- 1.2 A body corporate is a legal entity created under the Unit Titles Act 2010 when multiple owners have unit title properties in an apartment building or similar complex.¹ The body corporate comprises all the property owners and provides a way for the owners to act together in relation to their common and shared interests. This includes organising building maintenance, insurance, administration and financial management.
- 1.3 Currently, most bodies corporate are not registered for GST and Inland Revenue's historical position has been not to allow bodies corporate to register for GST. A High Court decision, *Taupo Ika Nui Body Corporate v CIR (1997) 18 NZTC 13,147*, appeared to support this position by suggesting that most residential bodies corporate would not be required to register for GST.
- 1.4 In recent years Inland Revenue has been asked to consider whether bodies corporate should be able to register for GST – in particular, by a small number of bodies corporate who consider they could be entitled to GST refunds (as their expenses have exceeded their fees).
- 1.5 To answer this question, Inland Revenue undertook a legal analysis and came to a view that, under the current law, a body corporate could be considered to carry on a taxable activity and make supplies to their owners in relation to a number of services required by the Unit Titles Act 2010.
- 1.6 A consequence of this view is that, if a body corporate makes supplies that exceed the \$60,000 threshold, it would be required to register for GST. Similarly, a body corporate that makes supplies below the threshold would be able to voluntarily register for GST.
- 1.7 The new interpretative view was consulted on in an issues paper, *IRRUIP7: Bodies corporate – GST registration* released in May 2013.

¹ In this document references to a "body corporate" refer to a body corporate of a unit title development created under section 75 of the Unit Titles Act 2010.

- 1.8 Many submissions on this issues paper raised policy arguments on why bodies corporate should not be required to register for GST. Concerns were raised that the outcome appeared inconsistent with the fact that other types of residential property owners (such as owners of stand-alone homes) are outside the GST system and cannot register for GST.² Other submissions pointed out that requiring bodies corporate to register for GST would impose compliance costs but, in most cases, would collect little additional tax revenue.
- 1.9 In response to these submissions, and concerns about the potential compliance costs that could arise under the new interpretation, the Government has decided to change the law so that it aligns the GST treatment with past operational practice and the GST treatment of other private homeowners.
- 1.10 For most bodies corporate, who have not registered for GST, the proposed changes would ensure that they would not have to take any action.
- 1.11 As part of the proposed changes, a “savings” provision will be provided for bodies corporate that are currently registered for GST. The savings provision will mean that these bodies corporate would apply the new rules from 6 June 2014 (the date the proposed changes were announced) and would apply the existing law for earlier periods.
- 1.12 Chapter 2 describes the technical details of the Government’s proposals and the intended policy outcomes of these proposals. To further clarify how the proposed rules might work, some suggested draft legislation has been prepared and presented in Appendix 1.

How to make a submission

- 1.13 The Government invites submissions on whether the proposed new rules and draft legislation would achieve the intended policy outcomes. Following analysis of these submissions, the Government intends to introduce amendments in the next available taxation bill.
- 1.14 Submissions should be addressed to:
GST treatment of bodies corporate
C/- Deputy Commissioner, Policy and Strategy
Inland Revenue Department
PO Box 2198
Wellington 6140
- Or email policy.webmaster@ird.govt.nz with “GST treatment of bodies corporate” in the subject line. Electronic submissions are encouraged. The closing date for submissions is Friday, 18 July 2014.

² In the case of an owner-occupier, GST does not apply as there is no supply for consideration when the homeowner provides accommodation to themselves. The GST Act exempts the supply of residential accommodation from GST to ensure that renters are not disadvantaged relative to owner occupiers.

- 1.15 Submissions may be the subject of a request under the Official Information Act 1982, which may result in their release. The withholding of particular submissions, or parts thereof, on the grounds of privacy, or commercial sensitivity, or for any other reason, will be determined in accordance with that Act. Those making a submission who consider that there is any part of it that should properly be withheld under the Act should clearly indicate this.

QUESTIONS FOR SUBMITTERS

1. A GST exemption is proposed to remove bodies corporate from the GST system from 6 June 2014 (the date the proposed changes were announced) and to ensure that those bodies corporate which have never registered for GST can never register. Would the proposed exemption achieve this result?
2. To preserve tax positions taken by bodies corporate that have been registered for GST before 6 June 2014 a “savings” provision has been developed. Would the savings provision be effective?
3. An optional rule is proposed to allow bodies corporate that have been registered for GST before 6 June 2014 to elect to be treated as being registered from GST from a certain date (1 April 2010). Would this rule work as intended?
4. Some bodies corporate would be de-registered for GST as a result of the proposed exemption and may be required to pay GST on any assets that they own. Is a transitional rule required to deal with this problem?
5. A look-through rule is proposed to eliminate the tax cascades that could otherwise arise when the underlying property owner is GST-registered. Would the proposed rule prevent tax cascades?

CHAPTER 2

Proposed new rules

- 2.1 This chapter describes the new rules that the Government is proposing to introduce. These include:
- a GST exemption to remove bodies corporate from the GST system;
 - a “look-through” rule to allow GST-registered unit owners to claim back GST on supplies provided to the body corporate by third parties (such as insurance) to the extent to which these relate to the unit owners’ taxable activity; and
 - a “savings” provision and date-of-registration rule that apply to bodies corporate that registered for GST before 6 June 2014 (the date the proposed changes were announced).
- 2.2 To further clarify how the proposed rules might work, suggested draft legislation has been prepared and presented in Appendix 1.

GST exemption for goods and services that a body corporate provides to its unit owners under the Unit Titles Act 2010

(Clause 1 / proposed new section 14(1)(f))

- 2.3 It is proposed that a supply provided by a body corporate to its unit owners will be an exempt supply for GST purposes.³
- 2.4 To be exempt, the supply must relate to a power or duty of the body corporate as listed in section 84 of the Unit Titles Act 2010. This requirement ensures that the new exemption does not create incentives for unit owners to arrange for their body corporate to provide them with a broader range of goods or services. For example, if the body corporate supplied meals, education or medical care, it would not be appropriate for these to be exempt supplies.
- 2.5 The proposed exemption should generally prevent bodies corporate from registering for GST. This is because they will not carry on a taxable activity in relation to their exempt supplies to unit owners and so will not be able to register for GST in relation to these activities.

³ In this document, references to a “body corporate” refer to a body corporate of a unit title development created under section 75 of the Unit Titles Act 2010.

- 2.6 The proposed exemption is designed to provide certainty and to eliminate the compliance costs that would otherwise arise if bodies corporate were required to register for GST. These compliance costs would have affected a large number of property owners. For example, if we assume a typical annual body corporate fee is around \$3,000, a body corporate comprising 20 or more units could have been required to register. Information from Land Information New Zealand suggests there are about 1,300 bodies corporate with 20 or more units, comprising around 72,000 unit owners who would potentially be affected. Inland Revenue has estimated that it costs small businesses about \$2,000 a year to comply with GST. This suggests that the potential total compliance cost savings could be around \$2.6 million a year.
- 2.7 It is likely that some bodies corporate are currently registered for GST. These bodies corporate will become de-registered as a result of the proposed exemption. In some cases this could lead to adverse consequences. For example, a body corporate may be required to pay GST on any assets they own. If problems do arise in practice, it is proposed that transitional rules could be developed to provide relief.
- 2.8 Some bodies corporate may carry on a separate taxable activity (such as a business venture) that is unconnected to providing goods and services to its unit owners under the Unit Titles Act. Under these circumstances, a body corporate could still register for GST, but the exempt supplies that they provide to their owners under the Unit Titles Act would not be included in their taxable activity. As a consequence, the body corporate would not be able to claim any input tax credits for any inputs used in making these exempt supplies.

Proposed application date

(Clause 1(2))

- 2.9 For a body corporate that has not actually been registered for GST before 6 June 2014, the exemption would apply from 1 October 1986. This would mean these bodies corporate would not be required to register for GST and, in fact, would not be able to register for GST at any point in time.

Savings provision for bodies corporate currently registered for GST

(Clause 1(2))

- 2.10 A “savings” provision will be provided for bodies corporate that are currently registered for GST. These bodies corporate would apply the new exemption from 6 June 2014 and apply the existing law for earlier periods.
- 2.11 The savings provision would apply to bodies corporate that have actually been registered for GST (so they have a GST number) before 6 June 2014.
- 2.12 The savings provision means the proposed exemption would not apply to tax positions that have been filed in GST returns before 6 June 2014.

- 2.13 The existing law provides the Commissioner of Inland Revenue with a discretion to determine the date that a person becomes registered for GST. (See section 51(4) of the Goods and Services Tax Act 1985.)
- 2.14 However, this discretion is unlikely to provide sufficient certainty for those bodies corporate that have registered for GST before 6 June 2014. This uncertainty is partly a result of the fact that the definition of a “registered person” includes a person who is liable to be registered for GST.
- 2.15 To provide certainty, an optional rule is proposed for bodies corporate that have registered for GST that will allow them to elect to be treated as being registered for GST from a certain date (usually 1 April 2010).

Date of registration for bodies corporate covered by the savings provision

(Clause 2 / proposed new sections 51(4B) and (4C))

- 2.16 The “date of registration” rule would apply to bodies corporate that registered for GST on a date between 1 April 2010 and 6 June 2014, and who would also be covered by the savings provision.
- 2.17 It would allow these bodies corporate to elect to be treated as being registered for GST from the later of:
- a) the date of their first taxable period beginning after 1 April 2010; or
 - b) the date that they first became liable to be registered for GST under section 51(1) of the GST Act 1985.
- 2.18 So, for example, if a body corporate became liable to register for GST in April 2012 they could only register from April 2012. If they became liable to register in 1998 they could only register from 1 April 2010.
- 2.19 Allowing these taxpayers to backdate their GST registration to April 2010 is broadly consistent with the four-year time-bar for amending a GST assessment in section 108A of the Tax Administration Act 1994.

Look-through rule to allow the underlying owners to claim input tax deductions if they are GST-registered

(Clause 3 / proposed new section 60C)

- 2.20 A potential concern with GST exemptions is that they can create “tax cascades” (where the total tax cost would increase with each additional step in the supply chain).
- 2.21 The GST system eliminates these tax cascades by allowing businesses to claim back the GST cost of their inputs.

- 2.22 For example, if a homeowner runs a GST-registered business from their home, such as workshop or home office, and they purchase house insurance they may be able to claim a GST input credit to the extent to which the insurance relates to the portion of the house that they use for their business.
- 2.23 In the case of a unit title property, the Unit Titles Act requires the body corporate to arrange insurance. In this scenario, a business may insure its business premises indirectly as part of its body corporate fees. Because there is no GST charged on the body corporate fee, the business may find itself unable to claim back the GST cost of the insurance.
- 2.24 To remove these tax cascades a “look-through” rule has been developed. The look-through rule would treat any supplies that are received by the body corporate (such as insurance or maintenance), to be provided directly to the underlying owners in proportion to each unit owners’ ownership interest in the body corporate.
- 2.25 The look-through rule would apply to supplies made after 6 June 2014.

APPENDIX 1

Suggested draft legislation

Submissions are sought on whether the suggested drafting presented below would achieve the intended policy outcomes described in chapter 2.

Following analysis of submissions, the Government intends to introduce amendments in the next available taxation bill.

1 Section 14 amended (Exempt supplies)

- (1) After section 14(1)(e), insert:
 - “(f) the supply of goods or services by a body corporate, as that term is defined in section 5 of the Unit Titles Act 2010, to the extent to which the goods or services are supplied under a power or duty of the body corporate as set out in section 84 of that Act.”
- (2) **Subsection (1)** applies for supplies made on or after 1 October 1986. However, **subsection (1)** does not apply—
 - (a) to a body corporate that is registered for GST before (*date of announcement*) as a result of an application under section 51(2) or 51(3); and
 - (b) for the period that starts on 1 October 1986 and ends on (*date of announcement*); and
 - (c) in relation to the tax treatment under the Goods and Services Tax Act 1985 of supplies made by the body corporate during the period.

2 Section 51 amended (Persons making supplies in course of taxable activity to be registered)

- (1) After section 51(4), insert:
 - “(4B) **Subsection (4C)** applies to a body corporate that is registered for GST between 1 April 2010 and (*date of announcement*) as a result of an application under section 51(2) or 51(3).
 - “(4C) Despite subsection (4), the body corporate may choose to be a registered person for the purposes of this Act with effect from the date that is the later of—
 - “(a) the first day of their first taxable period that occurs after 1 April 2010; or
 - “(b) the first day on which they are liable to be registered under subsection (1).”
- (2) **Subsection (1)** comes into force on (*date of announcement*).

3 New section 60C inserted (Bodies corporate)

(1) After section 60B, insert:

“60C Bodies corporate

“(1) To the extent to which a supply of goods or services made to a body corporate is used in the course of making an exempt supply under **section 14(1)(f)**, the supply is treated as made—

“(a) to the persons who are owners of the units and common property administered by the body corporate; and

“(b) in proportion to each unit owner’s ownership interest in the body corporate.

“(2) For the purposes of this section, **body corporate, common property, owner, ownership interest, and unit** have the meanings given in section 5 of the Unit Titles Act 2010.”

(2) **Subsection (1)** applies for supplies made on or after *(date of announcement)*.

(3) **Subsections (1) and (2)** come into force on *(date of announcement)*

APPENDIX 2

Current law

There are currently no specific rules for bodies corporate in the GST Act. The main rules for applying GST are set out below.

Goods and Services Tax Act 1985

Section 2(1) of the GST Act defines “consideration” as:

consideration, in relation to the supply of goods and services to any person, includes any payment made or any act or forbearance, whether or not voluntary, in respect of, in response to, or for the inducement of, the supply of any goods and services, whether by that person or by any other person; but does not include any payment made by any person as an unconditional gift to any non-profit body:

Section 6(1) of the GST Act defines “taxable activity” as:

6. Meaning of term “taxable activity”

- (1) For the purposes of this Act, the term taxable activity means—
 - (a) any activity which is carried on continuously or regularly by any person, whether or not for a pecuniary profit, and involves or is intended to involve, in whole or in part, the supply of goods and services to any other person for a consideration; and includes any such activity carried on in the form of a business, trade, manufacture, profession, vocation, association, or club:
 - (b) without limiting the generality of paragraph (a), the activities of any public authority or any local authority.

...

Section 8(1) of the GST Act collects GST from registered persons on their supplies of goods and services:

8 Imposition of goods and services tax on supply

- (1) Subject to this Act, a tax, to be known as goods and services tax, shall be charged in accordance with the provisions of this Act at the rate of 15% on the supply (but not including an exempt supply) in New Zealand of goods and services, on or after 1 October 1986, by a registered person in the course or furtherance of a taxable activity carried on by that person, by reference to the value of that supply.

Section 51 of the GST Act contains the rules for registering people for GST:

51 Persons making supplies in course of taxable activity to be registered

(1) Subject to this Act, every person who, on or after 1 October 1986, carries on any taxable activity and is not registered, becomes liable to be registered—

(a) at the end of any month where the total value of supplies made in New Zealand in that month and the 11 months immediately preceding that month in the course of carrying on all taxable activities has exceeded \$60,000 (or such larger amount as the Governor-General may, from time to time, by Order in Council declare):

provided that a person does not become liable to be registered by virtue of this paragraph where the Commissioner is satisfied that the value of those supplies in the period of 12 months beginning on the day after the last day of the period referred to in the said paragraph will not exceed that amount:

(b) at the commencement of any month where there are reasonable grounds for believing that the total value of the supplies to be made in New Zealand in that month and the 11 months immediately following that month will exceed the amount specified in paragraph (a):

provided that any such person shall not become liable where the Commissioner is satisfied that that value will exceed that amount in that period solely as a consequence of—

(c) any ending of, including a premature ending of, or any substantial and permanent reduction in the size or scale of, any taxable activity carried on by that person; or

(d) the replacement of any plant or other capital asset used in any taxable activity carried on by that person; or

(e) the supply, to persons who are non-residents but are physically present in New Zealand, of telecommunications services that are treated as being supplied in New Zealand under sections 8(6) and 8A.

(2) Every person who, by virtue of subsection (1), becomes liable to be registered shall apply to the Commissioner in the prescribed form for registration under this Act, within 21 days of becoming so liable, and provide the Commissioner with such further particulars as the Commissioner may require for the purpose of registering that person.

(3) Notwithstanding subsections (1) and (2), every person who satisfies the Commissioner that, on or after 1 October 1986,—

(a) that person is carrying on any taxable activity; or

(b) that person intends to carry on any taxable activity from a specified date,—

may apply to the Commissioner in the prescribed form for registration under this Act, and provide the Commissioner with such further particulars as the Commissioner may require for the purpose of registering that person.

- (4) Where any person has—
- (a) made application for registration pursuant to subsection (2), (3), or section 54B, and the Commissioner is satisfied that that person is eligible to be registered under this Act, that person shall be a registered person for the purposes of this Act with effect from such date as the Commissioner may determine; or
 - (b) not made application for registration pursuant to subsection (2), and the Commissioner is satisfied that that person is liable to be registered under this Act, that person shall be a registered person for the purposes of this Act with effect from the date on which that person first became liable to be registered under this Act: provided that the Commissioner may, having regard to the circumstances of the case, determine that person to be a registered person from such later date as the Commissioner considers equitable

Unit Titles Act 2010

Section 5 of the Unit Titles Act 2010 defines a body corporate:

body corporate means a body corporate of a unit title development created under section 75 on the deposit of a unit plan

Section 75 of the Unit Titles Act 2010 creates a body corporate as a legal entity separate from the unit owners:

75 Creation of body corporate

(1) When a unit plan is deposited under section 17 (and in the case of a staged development, when the first stage unit plan is deposited under section 24), a body corporate is created and is the body corporate for the unit title development created by the deposit of that unit plan.

(2) When a unit plan is deposited under section 21 (and in the case of a staged development, when the first stage unit plan is deposited under section 24), a subsidiary body corporate is created and is the body corporate for the subsidiary unit title development created by the deposit of that unit plan.

Section 84(1) of the Unit Titles Act 2010 sets out the powers and duties of the body corporate:

84 Powers and duties of body corporate

- (1) The body corporate has the powers and duties set out in—
- (a) sections 38 to 42 (which relate to the fixing and reassessment of the ownership interest and the utility interest):
 - (b) section 81 (which permits the body corporate to act as an agent for the unit owners who lease or licence their principal unit and are absent for the purpose of enforcing the body corporate operational rules):
 - (c) section 85 (which requires the body corporate to keep and maintain a register of all the owners of principal units and accessory units on the plan):

- (d) section 86 (which relates to the body corporate's power to sign documents on behalf of the owner):
- (e) section 87 (which requires the payment of ground rental to a lessor):
- (f) section 90 (which relates to the calling of general meetings):
- (g) section 105(3) (which requires the body corporate to comply with the body corporate operational rules):
- (h) section 108 (which is the general power of delegation):
- (i) sections 115 and 117 to 120 (which relate to the establishment and maintenance of the funds):
- (j) section 116 (which requires the body corporate to establish and maintain a long-term maintenance plan):
- (k) section 121 (which relates to the raising of amounts for each fund and the imposition of levies on the unit owners to establish and maintain each fund):
- (l) sections 130 and 131 (which relate to the spending, borrowing, and investing of money and the distribution of surplus money and property):
- (m) section 132 (which relates to the keeping of accounting records and submission of its yearly financial statements to an independent auditor):
- (n) section 135 (which relates to insurance of the buildings and other improvements on the land):
- (o) section 136(4) (which relates to the application of insurance moneys in or towards reinstatement of the development):
- (p) section 138 (which relates to repair and maintenance of the common property, assets designed for use in connection with the common property, infrastructure, and building elements and access for those purposes):
- (q) section 206 (which relates to the provision of records and documents on request from a unit owner):
- (r) any other provisions of this Act, any other Act, or the regulations that confer powers or duties on the body corporate and subject to any limitations to those powers and duties in this Act, any other Act, or the regulations.

Section 121 of the Unit Titles Act 2010 gives a body corporate the power to impose levies on owners. Subsections (1) and (2) provide:

121 Contributions to be levied on unit owners

(1) A body corporate may determine from time to time the amounts to be raised for each fund and impose levies on the owners of principal units to establish and maintain each fund.

(2) The levies must be calculated as follows:

(a) in the case of the operating account, long-term maintenance fund, and any contingency fund, in proportion to each unit owner's utility interest; and

(b) in the case of any capital improvement fund, in proportion to each unit owner's ownership interest.

The Unit Titles Act 1972 applied up until 1 October 2012 when it was repealed and replaced by the Unit Titles Act 2010. In particular, clause 219 of the Unit Titles Act 2010 means the 2010 Act now applies to pre-2010 Unit titles.

219 Existing unit title developments

(1) In this subpart, an existing unit title development means the stratum estates to which a particular unit plan within the meaning of the Unit Titles Act 1972 relates where the unit plan—

(a) was deposited before the commencement of this Act; and

(b) has not been cancelled.

(2) An existing unit title development is a unit title development under this Act and the body corporate for the unit plan that relates to that unit title development is, for the purposes of this Act and for all other purposes, the body corporate for that unit title development.