The Institute of
Chartered Accountants
in Australia

13 March 2012

Ms Brenda Berkeley
General Manager
Indirect Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

Attention: Ms Joanne Croft
By email: gstpolicyconsultations@treasury.gov.au

Dear Brenda

Exposure Draft – GST and Sale of a Corporation's Property by Mortgagee or Chargee

The Institute of Chartered Accountants in Australia (the Institute) welcomes the opportunity to provide comments on the exposure draft (ED) of Tax Laws Amendment (2012 Measures No. 3) Bill 2012: 'GST supplies by representatives who are creditors' (the Bill) and explanatory memorandum (EM). The ED is intended to clarify that Division 105 of the GST Act[1] operates to the exclusion of Division 58 of the GST Act where a mortgagee in possession or control sells the property of a corporation.

The Institute is the professional body for Chartered Accountants in Australia and members operating throughout the world. Representing more than 70,000 professionals and business leaders, the Institute has a pivotal role in upholding financial integrity in society. Members strive to uphold the profession's commitment to ethics and quality in everything they do, alongside an unwavering dedication to act in the public interest.

Chartered Accountants hold diverse positions across the business community, as well as in professional services, government, not-for-profit, education and academia. The leadership and business acumen of members underpin the Institute's deep knowledge base in a broad range of policy areas impacting the Australian economy and domestic and international capital markets. The Institute's members include many insolvency practitioners.

Background

The Institute has made multiple submissions to Treasury and the Board of Taxation in relation to improvements required for the GST legislation to appropriately deal with insolvency scenarios. In each of those submissions, the Institute has recommended that the priority of Division 105 versus the main insolvency provision (now Division 58 and previously Division 147) needs to be clarified. In some of those submissions, we have also pointed out the confusion that exists because of the different capacities in which insolvency practitioners can be appointed by mortgagees in possession.

[1] All references are to *A New Tax System (Goods and Services Tax) Act 1999*

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Comments on the ED

The Institute welcomes the proposed change clarifying that Division 105 takes priority over Division 58 for creditors who make supplies in satisfaction of debts owed to them (hereafter "mortgagees in possession"). We believe that it is likely that the proposed provisions will deal adequately with the common scenario where a mortgagee exercises its rights to take possession of and dispose of a single property through a real estate agent.

The Institute's concern, however, is that the proposed change amplifies the inconsistent treatment between that common scenario and more complex affairs where a mortgagee in possession appoints a qualified person at an insolvency firm to take control of and dispose of a mortgagor's property.

Whether the qualified person is appointed as a "receiver" or qualifies as a "controller" per the *Corporations Act 2001,* they are likely to constitute a "representative" per the definition of that term in section 195-1 of the GST Act. The current practice, and the Institute suggests the better interpretation of the current law, is that such a representative is bound to apply Division 58 and will continue to do so even if the proposed changes become law.

Thus, the current inconsistent practice, which is reinforced by the proposed changes, can be summarised as:

- Division 58 applies if the mortgagee in possession appoints a representative or if one is appointed by the Court, or:
- Division 105 applies if a representative is not appointed.

According to the draft EM accompanying the Bill, Division 105 is to be preferred as it has a substantially different registration and reporting requirements. We understand that the policy is for mortgagees in possession to have the lower compliance burden conferred by Division 105. Whether that lower compliance burden applies to and/or should be available to other representatives probably should be determined as a matter of policy but ultimately may not be important.

What is important is that the two divisions have different procedures to determine the incidence of GST liability. Those differences, which may be decisive, are:

- Division 105 – the mortgagee in possession has a taxable supply if the debtor would have had a taxable supply, had it made the supply.[2] The supply will not be taxable if the mortgagee in possession has received a written notice from the debtor stating that the supply would not have been taxable had they made it.[3] If the mortgagee in possession cannot obtain such a notice, it can treat the supply as not taxable if on the basis of reasonable information, it believes that the supply would not have been taxable had the debtor made it.[4]

- Division 58 – the representative needs to determine whether the incapacitated entity was GST registered or required to be registered and then registers itself accordingly. It then determines the liability on any sale of real property or other assets per section 9-5 and the various exemptions and concessions. Thus, the GST liability is determined solely by strict application of the law without room for subjective opinion or declaration.

[2] Para 105-5(b)
[3] Para 105-5(3)(a)
[4] Para 105-5(3)(b)

Because of this difference in determining the incidence of GST liability, the Institute foreshadows that what is currently a rare commercial practice may increase in some scenarios. The mortgagees in possession, primarily the banks, may appoint insolvency firms as their agent rather than have them appointed as representatives of the incapacitated entity. Then, the insolvency firm will not have liability for the GST. Rather, all of the gross proceeds from asset realisations will be controlled by the mortgagee in possession. Whether any GST liability is ultimately paid will be subject to the subjective determinations in section 105-5(3) and potentially to Corporations law responsibilities and no doubt other commercial considerations. It should be noted that, at least to the Institute's knowledge, there has not been a case which has conclusively demonstrated that the GST liability applying to a mortgagee in possession (under Division 105), takes priority over Corporations law responsibilities or other common law entitlements.

In summary, the Institute contemplates the proposed changes could accelerate the adoption of commercial practices by mortgagees which will result in less GST being paid where mortgagees foreclose because borrowers are unable to meet repayments where they fall due. Accordingly, we recommend that Treasury consider including in the amendment a proviso that removes or reduces the opportunity for Division 58 to be structured out of, such as through the use of agency arrangements, where it would have otherwise applied to an appointed insolvency practitioner.

We trust that the above comments are of assistance in finalising the ED. If you have any questions on any aspect of the submission, please contact Donna Bagnall on (02) 9290 5761 in the first instance to discuss.

Yours sincerely

Yasser El-Ansary
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The Institute of Chartered Accountants in Australia