NATIONAL INSTITUTE OF ACCOUNTANTS

26 January 2011

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

By email: marginscheme@treasury.gov.au

Dear Sir/Madam

Submission on implementation of the recommendations of Treasury's review of the GST margin scheme discussion paper

The National Institute of Accountants (NIA) is one of the three professional accounting bodies in Australia. The NIA has over 22,000 members who work in all areas of the accounting profession, including advising on taxation matters, superannuation and financial planning. In addition, two-thirds of the NIA's members work in and with small business.

We welcome the opportunity to provide this submission concerning the discussion paper on the implementation of the recommendations of Treasury's review of the GST margin scheme.

GST and Margin Scheme

Division 75 of the GST Act sets out special rules for real property that allows taxpayers an alternative means of calculating GST. The policy intent behind the margin scheme is to ensure that GST is payable only on the incremental value added to land by each registered entity, in a series of transactions after the land enters the GST system.

The policy objective of the margin scheme is to achieve three outcomes:

1. Exclude pre-1 July 2000 value from the taxable value of land;
2. Exclude post-1 July 2000 value added other than through a GST-registered enterprise from the tax base; and
3. Ensure that each supplier pays GST only on the value added by that supplier.

Unfortunately the margin scheme is not always achieving its policy objectives due to shortcomings in its scheme design. We acknowledge the significant challenges in a GST context in trying to devise a system that achieves the stated policy objectives.

This is due in part to the complexity that is common in property transactions as well as having to deal with conceptual differences between the legal definition of real property and its tangible attributes.

The current margin scheme regime results in complexity, uncertain outcomes and significant compliance costs. It's no surprise that the application of the margin

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scheme has resulted in a rising proportion of all GST litigation since its introduction back in 2000.

We acknowledge that the margin scheme represents a departure from the basic rules of GST law and therefore necessarily involves an additional level of complexity such as the need to obtain valuations of real property or to identify if the vendor is eligible to sell using the margin scheme.

Unfortunately, the policy objectives of the margin scheme legislation have been undermined by the amount of 'tinkering' since the GST was introduced. This has been brought about by attempts to protect the integrity of the margin scheme together with system design anomalies which are designed to achieve its policy aims.

Examples of where the current system falls short include:

- Application of GST to value added since 1 July 2000 that was not in the course of a GST registered enterprise.

- The application of GST on value added since the entity acquired the property and not on the value at the date of effect of its registration or the date on which the land was ventured into an enterprise.

- Having to look back at the treatment of past transactions by external unrelated parties to determine whether you are eligible to use the margin scheme. A system that requires tracing will inevitably create ongoing technical and practical application difficulties as well as costly compliance.

The discussion paper only intends to restructure the margin scheme provisions to give prominence to the core provisions with exceptions set out separately. It also intends to insert objects clauses for the key provisions so that the intention is clear. The discussion paper is proposing to implement a minor technical amendment to remove an anomaly to allow an approved valuation of the land to be used for the purposes of calculating the margin on subdivided land. All other known deficiencies of the margin scheme are to be retained.

Justification noted in the discussion paper for not addressing other industry concerns within the existing legislative framework was that it would have required additional rules increasing complexity. Treasury has acknowledged 'gaps' within the existing framework but has decided to live with these shortcomings in order not to complicate existing rules any further.

The retention of the current margin scheme design approach will not in our opinion alleviate the scheme's shortcomings. The replacement of the margin scheme with a simpler, more efficient model that is better able to deal with many of the fundamental challenges is our preferred option. There are alternative policy models for the GST treatment of property such as a notional input tax credit regime which warrants serious consideration and we urge the Government to seriously consider replacing the existing margin scheme system with a simpler more streamlined system to overcome anomalies and complexities of the current system.

A simpler more efficient mechanism such as a notional input tax credit regime that is subject to integrity rules should be considered as a viable alternative methodology in dealing with the complexities of applying GST to property transactions. The notional input tax credit system would alleviate many of the complexities as it delivers the intended input tax relief once at a single point rather than at each point down the supply chain, resulting in a simpler process of achieving intended policy outcomes. The repetitive mechanism required under the existing framework has the potential to create a multiplier-effect if errors occur along the supply chain. A notional input tax credit will ensure that only the final consumer incurs the GST cost on the amount of value added by registered persons along the supply chain, thereby avoiding any potential tax cascading to occur.

We would have preferred that the existing margin scheme be completely replaced with a simpler more streamlined alternative policy model that achieves the broad policy aims.

If you need further clarification on any of the matters raised above, please do not hesitate to contact me on 0419369038 or via email at tony.greco@nia.org.au.

Yours faithfully

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