



WEEKLY COMMENT: FRIDAY 13 FEBRUARY 2015

1. This week I take a last look at GST-related statements issued by Inland Revenue in the past months, before going on next week to round up the GST law amendments enacted in 2014. This week I look at:
 - (a) Public Ruling BR Pub 14/06 *Payments by parents or guardians of students to state schools – GST treatment* was released by Inland Revenue on 28 August 2014 and is published in *Tax Information Bulletin* Vol. 26, No. 9, October 2014, page 3. The subject matter was previously dealt with in BR Pub 09/01. The new ruling applies from 21 June 2013 to 20 June 2018.
 - (b) Question We've Been Asked QB 14/03 *GST – Transfer of interest in a partnership* is published in *Tax Information Bulletin* Vol. 26, No. 5, June 2014, page 3. It updates and replaces Question 108 published in *Public Information Bulletin* No. 158, November 1986 and *GST treatment of the sale of an interest in a taxable activity* published in *Public Information Bulletin* No. 164, August 1987.
 - (c) Product Ruling BR Prd 14/08 *Body Corporate 358851* released on 8 August 2014 and published in *Tax Information Bulletin* Vol. 26 No. 8 (September 2014) p. 4.
 - (d) A statement released by Inland Revenue and published in *Tax Information Bulletin* Vol. 27 No. 1 (February 2015) p. 43 concerning the current status of the withdrawal in *Tax Information Bulletin* Vol. 12, No. 5 (May 2000) of *GST – Matrimonial property agreements* previously published in *Tax Information Bulletin* Vol. 1, No. 6 (December 1989).

Payments by parents or guardians to state schools

2. Public Ruling BR Pub 14/06 *Payments by parents or guardians of students to state schools – GST treatment* concerns the circumstances in which such payments would constitute consideration for a supply and, therefore, be subject to GST.
3. Section 2 of the *Goods and Services Tax Act 1985* (“the GST Act”) provides that:
 - (a) “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; and
 - (b) “Consideration in money” includes consideration expressed as an amount of money.

4. BR 14/06 contains a discussion of the meaning of “consideration”. It is noted that:
 - (a) In *Turakina Maori Girls College Board of Trustees v CIR* (1993) 15 NZTC 10,032 (CA) McKay J noted that the supply could be to a person other than the person who provides the consideration. Likewise, the value of the supply is to be measured by the consideration, whether or not the consideration is provided by the person to whom the service is supplied. It is not necessary that there should be a contract between the supplier and the person providing the consideration, so long as the consideration is “in respect of, in response to, or for the inducement of, the supply”.
 - (b) The case of *The Trustee, Executors and Agency Co NZ Ltd v CIR* (1997) 18 NZTC 13,076 (HC) is referred to as providing support for the view that the supply could be made by someone other than the person who receives the payment, providing “there is sufficient proximity between the supply and payment”.
 - (c) Not all payments will be consideration:
 - (i) There must be a sufficient relationship between a payment and a supply of goods and services, and a distinction is drawn between a payment for a supply, and a payment in respect of a taxable activity. In *CIR v NZ Refining Co Ltd* (1997) 18 NZTC 13,187 (CA) Blanchard J said “It is necessary ... to distinguish between supplies and the taxable activity ... in the course of which they are made.”
 - (ii) It is not sufficient that the person who receives the payment carries out some activity that has the effect of benefiting either the person making the payment or some other person. In *Chatham Islands Enterprise Trust v CIR* (1999) 19 NZTC 15,075 (CA) a payment by the Crown to a trust established to promote economic development in the Chatham Islands was not consideration because the trustees were fulfilling their fiduciary duties under the trust, and the payment was not an inducement for the performance of services by the trustees.
 - (d) The legal arrangements between the parties will be very important. Blanchard J commented in the *Chatham Islands* case that because GST is a tax on transactions, it is necessary to pay close attention to the legal nature of what has been done.
5. In deciding whether a payment by a parent or guardian to a State school is a consideration for a supply, it is necessary to look into what such schools can actually charge parents for. Education Circular 2013/06 issued on 13 June 2013 prohibits Boards of Trustees of state and integrated schools from making any compulsory charges, other than attendance dues payable to proprietors of integrated schools and charges for voluntary purchase of goods and services from state schools. All other “charges” are essentially requests for donations, and are not compulsory.
6. Under s. 3 of the *Education Act 1989*, everyone who is not an international student (that is, generally, a New Zealand citizen or resident) is entitled to free enrolment and free education at any state school during the period beginning on their 5th birthday and ending on the 1st of January after their 19th birthday.
7. Under s. 35(1) of the *Private Schools Conditional Integration Act 1975*, students enrolled at an integrated school are entitled to free education on the same terms and conditions as students enrolled at other state schools. However, the proprietors of an integrated school may require payment of attendance dues as a condition of enrolment and attendance. The money received from attendance dues can be used only for improvements to the school

buildings and associated facilities as may be required by any integration agreement, for capital works, and to meet mortgage repayments relating to the school premises.

8. The policy of the *Education Act 1989* is to decentralise the administration of education so that Boards of Trustees of schools are responsible for the control and management of the schools. However, school Boards have an obligation to provide education that complies with the requirements of the national education guidelines. Every school must have a school charter, which establishes the missions, aims, objectives, directions and targets of the school Board that will give effect to the Government's national education guidelines and the Board's priorities.
9. The Commissioner's view, therefore, is that there is an insufficient relationship between any payments and the supply of education services. The supply of education services is not conditional on payment being made by parents and as students have a statutory right to receive education services in a state school free of charge if they are domestic students, there is an insufficient relationship between the payments and the supply of education services to which there is a statutory entitlement.
10. The situation is distinguished from that in *Television NZ Ltd v CIR* (1994) 16 NZTC 11,295 (HC) where payments the Department of Maori Affairs made to the Broadcasting Council for the purpose of a training scheme operated by the Broadcasting Council for Maori trainees were held to be payments for a supply for services, despite Television NZ's argument that it had a statutory obligation to promote the greater involvement of Maori as employees of the Broadcasting Council. There was a contractual obligation to provide the services, and the fact the supply was in accordance with the statutory obligations of the Broadcasting Council did not affect the conclusion that a supply was made under the contract.
11. In contrast, the payments made by parents are not made for any particular purpose and the school Boards do not undertake any obligations in return for payment. While there is an expectation that the amounts will be used for education purposes, school Boards have a considerable degree of autonomy as to how their funds are used. In any case, following the *Chatham Islands* and *Turakina* cases, how the amounts paid are used is not the test of whether a supply is made for the payment.
12. Moreover, there will be no supply of education services for a consideration even if a representation is made that education services would be withheld if payment is not made. This is because the true legal position is that education services would be provided whether or not the payment was made.
13. However, there will be a taxable supply if the supply made is outside the scope of the statutory entitlement and there is a sufficient relationship between the supply and the payment. This will be the case where students have a choice as to whether to receive the supply – for example, the optional purchase of materials such as workbooks and charges for in-school voluntary activities such as lunchtime sport or education outside the classroom opportunities.
14. In such cases, GST will be payable and the fact that, under s. 5(6) of the GST Act, Government grants to the school are a supply for GST purposes, does not affect any separate supply the Board makes to parents. The Court of Appeal recognised in *Suzuki NZ Ltd v CIR* [2001] NZCA 144, (2001) 20 NZTC 17,096 (CA) that when performance obligations under two separate contracts overlap a supply for GST purposes can occur simultaneously under both contracts.

Transfer of interest in a partnership

15. Question We've Been Asked QB 14/03 *GST – Transfer of interest in a partnership* covers the situation where an interest in a partnership is transferred from one partners to another new or existing partner.
16. A partnership is a “separate person” for GST purposes. This is despite the general law position that an unincorporated body of persons does not have a legal personality separate from its members. For GST purposes, an unincorporated body of persons, which is defined in s. 2 of the GST Act as including a partnership, is a separate person for GST purposes.
17. Therefore, if the only taxable activity a person is involved in is that carried on by a partnership, the person cannot register for GST.
18. A distinction is drawn between changes in the members of a partnership and transfers of interests in a partnership. Under s. 57(2)(e) of the GST Act, any change between members of a partnership has no effect for GST purposes. However, it is possible to have a change in partnership interests (through a rearrangement) even though there may be no change in the members.
19. Whether or not a supply of an interest in a partnership is subject to GST depends on:
 - (a) Whether the supplier is GST-registered in respect of a taxable activity; and
 - (b) Whether the supply is made in the course or furtherance of that taxable activity; and
 - (c) Whether the supply is a taxable or an exempt supply.
20. It is noted in QB 14/03 that the supply of a partnership interest will be a supply of a chose in action and, therefore, the supply of a service. It is not a supply of the underlying assets, and the nature of the underlying assets does not affect the characterisation of the supply as a standard-rated, exempt, or zero-rated supply. For example, the transfer of an interest in a land-owning partnership would not be zero-rated under s, 11(1)(mb) of the GST Act.
21. When an interest in a partnership is supplied by an existing partner, there will be a taxable supply for GST purposes if:
 - (a) The partner is registered for GST in their own right, because they carry on some other taxable activity (because the partner cannot register for GST for the activities of the partnership); and
 - (b) The interest in the partnership is supplied in the course or furtherance of that other taxable activity – i.e. the partnership interest is held, and then transferred, in the course or furtherance of the taxable activity carried on by the partner in their individual capacity, or the partner could carry on a taxable activity of buying and selling partnership interests; and
 - (c) The supply is not an exempt supply – i.e. the supply of the partnership interest is not a supply of a participatory security or an equity security.
22. The supply of a partnership interest will be the supply of a participatory security, as defined in s. 3(2) of the GST Act and, therefore, an exempt supply if:
 - (a) The partnership interest is an interest or right to participate in the capital, assets, earnings, or other property of any person (in the Commissioner's view this requirement is met); and

- (b) It is not an equity security (in which case it is separately exempt), a debt security, money or a cheque (and these requirements will be met as a partnership interest is not a right to be paid money that is owing, and is neither “money” nor “cheques”); and
 - (c) The partnership interest is a contributory scheme as defined in section 2 of the *Securities Act 1978* (repealed), which is a scheme that involves the investment of money and involves more than 5 investors or the manager manages other such arrangements (in the Commissioner’s view an interest in a partnership that involves an investment in money and meets the size threshold will meet this requirement).
23. The supply of an interest in a partnership will be the supply of an equity security, as defined in s. 2 of the GST Act, if it is an interest in or right to share in the capital of a body corporate. The Commissioner’s view is that a limited partnership registered under s. 51 of the *Limited Partnerships Act 2008* is a separate legal person and a “body corporate” for the purposes of the GST Act.
24. QB 14/03 contains 3 fairly simple examples that illustrate the above principles.

GST treatment of insurance payment

25. Product Ruling BR Prd 14/08 *Body Corporate 358851* concerns the GST treatment of a payment received by unit owners from their body corporate which received an insurance payment following the Canterbury earthquakes. The body corporate resolved not to reinstate the building and to distribute the material damage portion of the insurance payment (net of certain costs) to owners of units, the majority of whom were GST-registered.
26. The ruling states that:
- (a) The insurance payment made by the insurer to the body corporate under the settlement agreement is not an insurance payment received in the course or furtherance of a taxable activity by a GST-registered owner for the purposes of s. 5(13) of the GST Act; and
 - (b) A distribution by the body corporate to a GST registered owner is not a payment received by a GST registered owner under a contract of insurance for the purposes of s 5(13); and
 - (c) A distribution by the body corporate to a GST registered owner is not consideration for a taxable supply made by the owner to the body corporate for the purposes of s 8 of the GST Act; and
 - (d) A distribution by the body corporate to a GST registered owner is not consideration for a taxable supply made by the owner to the Canterbury Earthquake Recovery Authority (CERA) for the purposes of s 8; and
 - (e) Section 76 (tax avoidance) does not apply.

Relationship property agreements – GST implications

27. The Commissioner released a statement on 4 December 2014 stating that ordinary GST provisions and principles would apply to situations where a GST-registered sole trader transferred an interest in their taxable activity to their relationship partner.
28. This followed the withdrawal in 2000 of Inland Revenue’s previously published view in 1989 that relationship partners had always jointly owned the assets and a partnership was presumed to have existed between them. The Commissioner no longer considered that was correct.

29. It is noted in the article that companies and trusts are now more commonly involved as trading entities than was previously the case. The GST issues are less complicated as a result. Often the taxable activity is transferred as a going concern, or shares in a company are transferred without GST consequences (being an exempt supply).
30. Apparently, therefore, the situation involving the transfer of an interest in a taxable activity covered in the withdrawn TIB item rarely occurs in practice. Therefore, no further resources are being allocated to this matter.



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