

August 2010

Look out for farmers

This article appeared in this month's edition of the Law Society Journal (NSW).

Your good friend and client Peter rings up and asks you to act for him on a sale. Peter is a solo accountant and a bit of a wheeler-dealer. You do a fair bit of work for him and ask him what is the go this time. He says that he has this farm up in the bush that has been doing pretty well, but he has received a good offer and would like to sell it. You have a busy suburban practice with lots of real estate, but not much in the way of farms. Peter is a good client, though, and you don't like to say no. So you say yes.

Peter tells you that the sale of farms is a GST free exercise, so when preparing the contract you tick the appropriate boxes.

In the course of the matter, when talking to the buyer's solicitor in the normal way, you mention that you don't do many farms. As it happens, neither does the buyer's solicitor, who mentions that his client is really a property developer who intends to use property for a residential subdivision. The sale proceeds smoothly and is settled in due course. Peter is happy.

The sting

A few months later Peter telephones to say that he is subject to a GST audit. One of the questions raised by the auditor is whether the farm sale was truly GST free. As Peter says, to be GST free not only must the land have been used for a farm business before the sale but also the purchaser must have intended to use the land for a farming business after the sale. He then asks for a copy of the warranty in the contract verifying the purchaser's intention.

Your understandable immediate reaction is to quietly panic but to say "sure, I'll look into it and get back to you mate". You hope the standard contract covers the situation in clause 13. You look at clause 13.7.1 dealing with sales that are not taxable supplies and which contains a promise by the purchaser that the property will not be used in a way that could make the sale taxable. You assume this covers and send him a copy with a quiet sigh of relief.

Unfortunately, a few days later you receive another telephone call from Peter. He says the auditor is still unsatisfied because the ATO is aware that the purchaser started the sale and subdivision process immediately after completion and has never used the property as a farm. The auditor wants better evidence of intention.

At this stage you call for help from a solicitor you know with expertise in the GST area. He soon points out the ATO's published views on the matter in the Primary Production Industry Partnership Issues Register on the ATO website. Paragraph 6.2.4 deals with the question of what, if any, documentary evidence is necessary to show the intention of the purchaser that farmland is to be used to carry on a farming business.

The answer is that a reasonable enquiry should be made which requires the vendor to ask the purchaser about their intention. The ATO recognises that, generally speaking, a written statement or warranty from

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the purchaser to that effect is enough. However, this doesn't apply where a vendor has reason to believe the information is incorrect.

This is the potential issue. The warranty was in standard form. No other enquiry was made. And you had that conversation about the purchaser's real intention.

Therefore, Peter has a problem. The four positive requirements in section 9.5 for a sale to be subject to GST are present: the sale is for consideration, it is made in the course or furtherance of the farming enterprise, it is connected with Australian land and Peter is registered for GST purposes. Neither of the two negative conditions are present, in that the supply is not GST free and it is not input taxed.

If you have paid GST in running a business you will still pay GST in winding it up. It is not a requirement that Peter be registered for GST purposes as a farmer. Registration as an accountant is sufficient.

Well, Peter, you say, under special conditions 13.7.2 the purchaser must pay a top-up for GST if it turns out that his promise in the standard clause was untrue. True enough, but the clause requires the payment to be made on completion and completion is long gone. Peter is not happy.

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